DATES: Effective August 24, 1987. This AD was effective earlier to all recipients of telegraphic AD T87-15-51, dated July 22, 1987.

ADDRESSES: The applicable service information may be obtained from Lockheed-California Company, P.O. Box 551, Burbank, California 91520, Attention: Commercial Order Administration, Dept. 65-33, U-33, B-1. This information may be examined at the FAA, Northwest Mountain Region, 17900 Pacific Highway South, Seattle, Washington, or at the Los Angeles Aircraft Certification Office, 4344 Donald Douglas Drive, Long Beach, California.

FOR FURTHER INFORMATION CONTACT: Mr. Augusto Coo, Aerospace Engineer, Airframe Branch, ANM-121L, FAA, Northwest Mountain Region, Los Angeles Aircraft Certification Office, 4344 Donald Douglas Drive, Long Beach, California 90808; telephone (213) 514-6319.

SUPPLEMENTARY INFORMATION: On July 22, 1987, the FAA issued telegraphic AD T87-15-51, applicable to Lockheed-California Model L-1011-385 series airplanes, which requires repetitive ultrasonic inspections for cracking of the inboard retract lugs of both the left and right main landing gear (MLG) shock strut cylinder, and repair or replacement, if necessary. This action was prompted by the report of an accident where, during roll-out after landing, the right-hand MLG on a Model L-1011-385 airplane collapsed and separated from the aircraft. The failure was attributed to a stress corrosion crack emanating from the bore of the inboard retract actuator lug on the right-hand MLG strut cylinder. This condition, if not corrected, could result in structural failure of the MLG shock strut cylinder and ultimate failure of the MLG.

Preliminary investigation of the aforementioned accident revealed that the strut cylinder lug bushing installed was was made of stainless steel and is the type of bushing the installation of which constitutes terminating action for the repetitive inspection requirements of AD 82-10-52-R1, Amendment 39-4671 (48 FR 29470; June 27, 1983). That AD was issued to require repetitive visual and/or ultrasonic inspections for cracks of the inboard retract actuator lug on both MLG strut cylinders of all Model L-1011-385 series airplanes; installation of a stainless steel strut cylinder lug bushing was provided as an optional terminating action for the required repetitive inspections. In light of the recent accident that has prompted this amendment, the FAA may consider further rulemaking action to amend the requirements of AD 82-10-52-R1.

Since this condition may exist or develop on other airplanes of this same type design, this AD requires, within 10 days after the effective date of this amendment, an initial ultrasonic inspection of the inboard retract lugs of both the left and right MLG shock strut cylinder on Model L-1011-385 series airplanes equipped with stainless steel bushings in the retract lugs, and repetitive inspections thereafter at intervals not to exceed 400 landings. Any MLG shock strut cylinder found to be cracked must be repaired or replaced in a manner approved by the FAA prior to further flight.

Since a situation existed, and still exists, that requires immediate adoption of this regulation, it is found that notice and public procedure hereon are impracticable, and good cause exists for making this amendment effective in less than 30 days.

The Federal Aviation Administration has determined that this regulation is an emergency regulation that is not considered to be major under Executive Order 12291. It is impracticable for the agency to follow the procedures of Order 12291 with respect to this rule since the rule must be issued immediately to correct an unsafe condition in aircraft. It has been further determined that this document involves an emergency regulation under DOT Regulatory Policies and Procedures (44 FR 11034; February 26, 1979). If this action is subsequently determined to involve a significant/major regulation, a final regulatory evaluation or analysis, as appropriate, will be prepared and placed in the regulatory docket (otherwise, an evaluation or analysis is not required).

List of Subjects in 14 CFR Part 39

Aviation safety, Aircraft.

Adoption of the Amendment

Accordingly, pursuant to the authority delegated to me by the Administrator, the Federal Aviation Administration amends § 39.13 of Part 39 of the Federal Aviation Regulations as follows:

PART 39—[AMENDED]

1. The authority citation for Part 39 continues to read as follows:

Authority: 49 U.S.C. 1354(a), 1421 and 1423; 49 U.S.C. 106(g) (Revised Pub. L. 97-449, January 12, 1983); and 14 CFR 11.89.

§ 39.13 [Amended]

2. By adding the following new airworthiness directive:

Lockheed-California Company: Applies to Lockheed-California Model L-1011-385 series airplanes, certificated in any category, which have stainless steel bushings installed in the retract lugs of the left and/or the right main landing gear (MLG) shock strut cylinder. Compliance required as indicated, unless previously accomplished.

To detect cracks and prevent structural failure of the MLG shock strut cylinder, accomplish the following:

A. Within 10 days after the effective date of this AD, unless previously accomplished within the last 400 landings, and thereafter at intervals not to exceed 400 landings, perform an ultrasonic inspection of the inboard retract lugs of both the left and right MLG shock strut cylinder, following the procedure specified in Section 2, Accomplishment Instructions, of Lockheed-California L-1011 Service Bulletin 093-32-A211, Revision 1, dated October 26, 1982, or later revisions approved by the Manager, Los Angeles Aircraft Certification Office, FAA, Northwest Mountain Region.

B. Any MLG shock strut cylinders that are found cracked must be repaired or replaced prior to further flight, in a manner approved by the Manager, Los Angeles Aircraft Certification Office, FAA, Northwest Mountain Region.

C. Alternate means of compliance which provide an acceptable level of safety may be used when approved by the Manager, Los Angeles Aircraft Certification Office, FAA, Northwest Mountain Region.

D. Special flight permits may be issued in accordance with FAR 21.197 and 21.199 to operate airplanes to a base in order to comply with the inspection requirements of this AD.

All persons affected by this directive who have not already received the appropriate service document from the manufacturer, may obtain copies upon request to Lockheed-California Company, P.O. Box 551, Burbank, California 91520, Attention: Commercial Order Administration, Dept. 65-33, U-33, B-1. This document may be examined at the FAA, Northwest Mountain Region, 17900 Pacific Highway South, Seattle, Washington, or 4344 Donald Douglas Drive, Long Beach, California.

This amendment becomes effective August 24, 1987.

It was effective earlier to all recipients of Telegraphic AD T87-15-51, issued July 22, 1987.

Issued in Seattle, Washington, on July 29, 1987.

Wayne J. Barlow,

Director, Northwest Mountain Region.

[FR Doc. 87-17690 Filed 8-4-87; 8:45 am]

BILLING CODE 4910-13-M

14 CFR Part 39

[Docket No. 87-NM-27-AD; Amdt. 39-5699]

Airworthiness Directives; Short Brothers Model SD3-60 Series Airplanes

AGENCY: Federal Aviation Administration (FAA), DOT.

ACTION: Final rule.

SUMMARY: This amendment adopts a new airworthiness directive (AD), applicable to certain Short Brothers Model SD3-60 series airplanes, which requires repetitive inspection of the spar webs of the horizontal stabilizer, and repair if cracks are found. This amendment is prompted by results of extended fatigue testing by the manufacturer, which revealed cracks in the spar web of the horizontal stabilizers. This condition, if not corrected, could result in loss of the structural integrity of the horizontal stabilizer.

EFFECTIVE DATE: September 10, 1987.

ADDRESSES: The applicable service information may be obtained from Short Brothers Aircraft, 2011 Crystal Drive, Suite 713, Arlington, Virginia 22202-3702. This information may be examined at the FAA, Northwest Mountain Region, 17900 Pacific Highway South, Seattle, Washington, or the Seattle Aircraft Certification Office, 9010 East Marginal Way South, Seattle, Washington.

FOR FURTHER INFORMATION CONTACT: Ms. Judy Golder, Standardization Branch, ANM-113; telephone (206) 431-1967. Mailing address: FAA, Northwest Mountain Region, 17900 Pacific Highway South, C-68966, Seattle, Washington 98168.

SUPPLEMENTARY INFORMATION: A proposal to amend Part 39 of the Federal Aviation Regulations to include an airworthiness directive, which requires repetitive inspections of the spar webs of the horizontal stabilizer on Short Brothers Model SD3-60 series airplanes, and repair if cracks are found, was published in the **Federal Register** on April 14, 1987 (52 FR 11998).

Interested parties have been afforded an opportunity to participate in the making of this amendment. No comments were received in response to the proposal.

After issuance of the proposal, Short Brothers issued Revision 3 to Service Bulletin SD360-55-11, dated April 28, 1987. This revision of the service bulletin differs from the original issue in that the initial compliance time for inspection has been extended from 8,000 flights to 12,000 flights for certain serial-numbered airplanes and other airplanes which have used 15° take-off flaps, and the number of flights between inspections has been extended from 1,000 flights to 1,500 flights. The final rule has been revised to reflect the compliance time and repetitive inspection intervals as indicated in Revision 3 to the Short Brothers service bulletin. The FAA has determined that this change will not have a significant adverse effect on the safety of flight, and will not impose any additional economic burden on operators.

After careful review of the available data, the FAA has determined that air safety and the public interest require the adoption of the rule with the changes noted above.

It is estimated that 33 airplanes of U.S. registry will be affected by this AD, that it will take approximately 5 manhours per airplane to accomplish the required actions, and that the average labor cost will be $40 per manhour. Based on these figures, the total cost impact of this AD to U.S. operators is estimated to be $6,600.

For the reasons discussed above, the FAA has determined that this regulation is not considered to be major under Executive Order 12291 or significant under DOT Regulatory Policies and Procedures (44 FR 11034; February 26, 1979) and it is further certified under the criteria of the Regulatory Flexibility Act that this rule will not have a significant economic effect on a substantial number of small entities because of the minimal cost of compliance per airplane ($200). A final evaluation has been prepared for this regulation and has been placed in the docket.

List of Subjects in 14 CFR Part 39

Aviation safety, Aircraft.

Adoption of the Amendment

Accordingly, pursuant to the authority delegated to me by the Administrator, the Federal Aviation Administration amends § 39.13 of Part 39 of the Federal Aviation Regulations as follows:

PART 39—[AMENDED]

1. The authority citation for Part 39 continues to read as follows:

Authority: 49 U.S.C. 1354(a), 1421 and 1423; 49 U.S.C. 106(g) (Revised Pub. L. 97-449, January 12, 1983); and 14 CFR 11.89.

§ 39.13 [Amended]

2. By adding the following new airworthiness directive:

Short Brothers PLC: Applies to Model SD3-60 airplanes, serial numbers SH3601 through SH3691 and SH3694, certificated in any category. Compliance required as indicated, unless previously accomplished.

To prevent loss of the structural integrity of the horizontal stabilizer accomplish the following:

A. Visually inspect, in accordance with the schedule listed below, the forward face of the rear spar web and the aft face of the front spar web for cracks between fuselage attach fitting at 12.5" left and right of the airplane center line, in accordance with Short Brothers Model SD3-60 Service Bulletin SD360-55-11, Revision 3, dated April 28, 1987.

1. For airplanes serial numbers SH3680 through SH3691 and SH3694, and airplanes which have used only 15° flap take-off since before or upon reaching 5,000 flights, inspection is required within the next 100 flights or prior to the accumulation of 12,000 flights, whichever occurs later. Repeat the inspection at intervals not to exceed 1,500 flights.

2. For all other airplanes, inspection is required within the next 100 flights or prior to the accumulation of 8,000 flights, whichever occurs later. Repeat the inspection at intervals not to exceed 1,000 flights.

B. If cracks are found, prior to further flight, modify by strengthening the horizontal stabilizer in accordance with Short Brothers Model SD3-60 Service Bulletin SD360-55-12, dated April 1986.

C. The repetitive inspections required by paragraph A., above, may be terminated following completion of the modification described in Short Brothers Model SD3-60 Service Bulletin SD360-55-12, dated April 1986.

D. An alternate means of compliance or adjustment of the compliance time, which provides an acceptable level of safety, may be used when approved by the Manager, Standardization Branch, ANM-113, FAA, Northwest Mountain Region.

E. Special flight permits may be issued in accordance with FAR 21.197 and 21.199 to operate airplanes to a base for the accomplishment of the inspections and/or modifications required by this AD.

All persons affected by this directive who have not already received the appropriate service documents from the manufacturer may obtain copies upon request to Short Brothers Aircraft, 2011 Crystal Drive, Suite 713, Arlington, Virginia 22202-3702. These documents may be examined at the FAA, Northwest Mountain Region, 17900 Pacific Highway South, Seattle, Washington, or the Seattle Aircraft Certification Office, 9010 East Marginal Way South, Seattle, Washington.

This amendment becomes effective September 10, 1987.

Issued in Seattle, Washington, on July 28, 1987.

Wayne J. Barlow,

Director, Northwest Mountain Region.

[FR Doc. 87-17691 Filed 8-4-87; 8:45 am]

BILLING CODE 4910-13-M

CONSUMER PRODUCT SAFETY COMMISSION

16 CFR Part 1015

Freedom of Information Act Regulations; Final Amendments on Fees

AGENCY: Consumer Product Safety Commission.

ACTION: Final amendments.

SUMMARY: When members of the public are provided documents under the Freedom of Information Act, the Commission may impose fees for such services as duplication and searching. The Commission is amending its regulations so that (1) the fees will reflect more accurately the Commission's direct (actual) costs of providing the services and (2) the fees will conform to the Freedom of Information Reform Act of 1986.

DATES: The amendments will become effective on September 4, 1987.

FOR FURTHER INFORMATION CONTACT: Alan Shakin, Office of the General Counsel, Consumer Product Safety Commission, Washington, DC 20207; telephone (301) 492-6980.

SUPPLEMENTARY INFORMATION:

A. Background

The Commission's existing regulations on Freedom of Information Act (FOIA) fees appear at 16 CFR 1015.9. They provide, in essence, that fees will be charged for FOIA services, but "certain information provided routinely in the normal course of doing business will be provided at no charge" (§ 1015.9(a)); that the Commission's Secretary determines and levies fees and may waive or reduce them "when the furnishing of the information can be considered as primarily benefiting the general public or when special circumstances warrant" (§ 1015.9(b)); that the Secretary's determination of fees may be appealed to the commission (§ 1015.9(b)); that the first $25 of fees will be waived (§ 1015.9(c)); and that fees are not levied where the requested documents are not provided or made available (§ 1015.9(d)).

The existing regulations also direct that payment should be by check or money order payable to the Consumer Product Safety Commission (§ 1015.9(e)). Finally, they set forth the schedule of charges for FOIA services: searches, computer time, reproduction, postage, microfiche, and microfilm (§ 1015.9(f)).

In October 1986 the Commission voted to propose certain changes to these FOIA fee regulations. Before it did so, however, the Freedom of Information Reform Act of 1986 ("Reform Act," at sections 1802-04 of Pub. L. 99-570, the Anti-Drug Abuse Act of 1986) was enacted.

The Commission's reasons for wanting to amend its FOIA fee provisions were to make the fees better reflect the direct (actual) costs of responding to FOIA requests and to clarify some provisions. The Reform Act addresses the direct-costs issue and other issues that require changes to the Commission's fee provisions.

On March 27, 1987 the Office of Management and Budget issued its final Fee Schedule and Guidelines ("OMB Guidelines") which the Reform Act required OMB to issue. 52 FR 10011. On April 2, 1987 the Department of Justice's Office of Legal Policy issued a memorandum on New FOIA Fee Waiver Policy Guidance ("DOJ Memorandum"). After considering the guidance provided in these OMB and DOJ documents, the Commission proposed amendments to its FOIA fee regulations on May 12, 1987. 52 FR 17767.

B. Public Comments

The Commission received one public comment on its proposed FOIA fee amendments. This comment, from attorneys for Public Citizen and the Freedom of Information Clearinghouse ("Public Citizen"), did not specifically address the Commission's proposal—rather, it discussed issues raised by the Reform Act, its legislative history, the OMB Guidelines, and the DOJ Memorandum. The Commission has considered Public Citizen's applicable points and addresses them in section C, below.

C. Final Amendments

This section summarizes the final amendments issued below, discusses their rationales, and explains the changes made to the proposed amendments (the citations are to the final amendments):

1. The Commission will provide certain routine information at no charge; otherwise, the Secretary will determine and levy FOIA fees in accordance with the regulations (§ 1015.9(a)). This provision shortens, but does not change, existing provisions.

2. Checks and money orders will be payable to the Treasury of the United States, instead of to the CPSC, but will continue to be sent to the CPSC (§ 1015.9(b)). This will make fee collection administratively easier because the U.S. Treasury eventually receives funds collected for FOIA responses.

3. Under the Reform Act, different categories of requests incur different types of costs. The four types of requests are: (a) Commercial use requests; (b) requests from educational and non-commercial scientific institutions; (c) requests from representatives of the news media; and (d) all other requests. The three types of costs are duplication, search, and review.

The Commission specifically sought comment on the issue of whether lawyers would be "commercial use requesters" or "other" requesters when seeking information under FOIA for use in product liability lawsuits. Although no public comments addressed this issue, the Commission has evaluated arguments on both sides, considered the positions taken by other federal agencies, and decided to apply the following criteria to requests from lawyers:

(a) If a FOIA request from a lawyer is being submitted on behalf of a client, the Commission will consider the client's use of the information to determine the proper category for that request. If the client is a victim seeking reimbursement for injuries suffered in an incident involving a consumer product, the request will be an "other" request and not a "commercial use" request. For clients in different categories, the intended use of the information will determine the type of request for fee purposes.

(b) If a FOIA request from a lawyer doesn't identify a client, the Commission will attempt to find out—for example, by telephoning the lawyer—if the request was submitted on behalf of a client.

(c) If the lawyer is not representing a client or refuses to reveal the client's identity, the lawyer's intended use of the information will determine whether the request is a "commercial use" request or some other type.

(d) For FOIA fee purposes, lawyers may identify their clients by category rather than by name. To assess appropriate fees, however, the Commission may insist on a specific description of the intended use.

4. To reflect and clarify the approach of categorizing requests from lawyers according to their clients' intended use of the information (whenever possible), the Commission has modified its definition of "commercial use request." As proposed, the definition referred to "a request from or on behalf of one who

seeks information for a use or purpose that furthers the commercial, trade, or profit interests of the requester or the person on whose behalf the request is made." The final definition refers, more simply, to a request that seeks information for a use or purpose that furthers commercial, trade, or profit interests (§ 1015.9(c)(v)).

Public Citizen sought a definition for "commercial use request" that would "[draw] a bright line between private, profit-making and non-profit entities." This seemed to be a request for a blanket guarantee that no request from public interest or non-profit organizations would ever be categorized as a commercial use request. The Commission believes that a fairer and more workable approach is to consider—for each FOIA request on an individual basis—how the information is intended to be used.

The statutory language of the Reform Act supports this approach by directing agency regulations to "provide that . . . fees shall be limited to reasonable standard charges for document search, duplication, and review, when records are requested *for commercial use*." 5 U.S.C. 552(a)(4)(A)(ii), as amended (emphasis added). The Act does not refer to commercial or other types of *users*. While FOIA requests from non-profit groups are unlikely to be commercial requests, the Commission will categorize them on a case-by-case basis.

5. Public Citizen suggested definitions for "educational institution" and "representative of the news media." The Commission's proposed definition of "educational institution," taken from the OMB Guidelines, listed the types of schools it included. Public Citizen's suggestion was that the Tax Code contains a better definition: entities "organized and operated exclusively for . . . educational purposes." The Commission is adopting a final definition that is based on this language (§ 1015.9(c)(vi)), but will not be bound by any tax law authorities in interpreting it.

Similarly, the Commission is changing its definition of "representative of the news media," in response to Public Citizen's comment, to "any person or organization which regularly publishes or disseminates news to the public, in print or electronically (§ 1015.9(c)(viii)). The proposed definition unfairly excluded free-lance journalists who are not associated with any specific news organization, and the final definition remedies that problem. Public Citizen also suggested broadening the definition to those who publish or disseminate information, rather than news, to the public. However, the Commission retained the word "news" in the definition because it is based on the statutory phrase "news media." "Information" is so broad that it might apply to people and organizations outside of the generally understood category of the news media.

All but one of the remaining definitions are being issued in final form as they were proposed (§ 1015.9(c) (i), (ii), (iii), and (iv)). The definition of "non-commercial scientific institution" has been rewerded for clarity, but the Commission intends its meaning to remain unchanged.

6. Commercial use requesters may be charged for duplication, search, and review costs; educational institution and non-commercial scientific institution requesters and representatives of the news media may be charged for duplication costs; and all other requesters may be charged for duplication and search costs (§ 1015.9(d)). The following discussion illustrates how the Commission intends to impose review costs under the amendments:

Section 6(b) of the Consumer Product Safety Act (15 U.S.C. 2055(b)) requires the Commission to give manufacturing and private labeling firms the opportunity to comment on documents in which they are identified. The Commission then reviews those comments and decides whether to withhold the documents. If so, the documents are often withheld because of a specific statutory provision, section 6(b), which makes them exempt from disclosure under Exemption 3 of the FOIA (5 U.S.C. 552(b)(3)).

The time spent processing documents under section 6(b) of the CPSA would be a "review" cost under the amendments, since "review" is defined to include the examination of documents to determine whether they are permitted to be withheld. Depending on the nature and length of the firms' comments, such review time is sometimes considerable.

7. Some changes are being made to the fee structure (§ 1015.9(e)), to make fees reflect direct (actual) costs more closely than the existing fees do:

(a) The cost of a search does not now depend on what type of employee conducted it. Under the amendments, clerical personnel will be "billed out" at one rate ($3.00 for each 15-minute period), while non-clerical and professional and managerial personnel will be billed out at a higher rate ($4.90 for each 15-minute period). In addition, any special costs of sending records from field locations to headquarters for review will be included in search fees, at the clerical rate.

(b) Computer time rates are being revised. Postage will be charged, on a direct-cost basis, only for special handling. The rates for materials and services not specified in the regulations will be on direct-cost bases, as determined by the Secretary.

(c) The costs of review, which are not currently charged, will be billed at $4.90 for each 15-minute period, since lawyers and other professionals perform this work.

8. The Reform Act addresses the circumstances under which agencies must waive FOIA fees. First, 100 pages of duplication and two hours of search time must be waived, except for commercial users. Second, fees must be waived (or, in rare cases, reduced) if disclosure of the requested information is in the public interest, because it is likely to contribute significantly to public understanding of the operations or activities of the government and is not primarily in the commercial interest of the requester.

The Commission currently waives the first $25 of fees for all requests. It also directs the Secretary to waive or reduce fees when the disclosure would primarily benefit the general public or when special circumstances warrant. These provisions are being amended as follows:

For commercial use requests, there will be no automatic waiver (§ 1015.9(f)(i)). For educational institutions, noncommercial scientific institutions, and representatives of the media (for which the Commission only imposes duplication costs), there will be a $10 waiver for duplication costs (at $.10/page, 100 pages of duplication would cost $10) (§ 1015.9(f)(ii)). For any other requester (for which the Commission imposes duplication and search costs), the waiver will be $10 for duplication costs and $40 for search costs (§ 1015.9(f)(iii)). The cost of a two-hour search would vary, depending on the status of the employee searcher, from $24.00 to $39.20 (computer searches are excluded). For administrative convenience, the Commission will waive the highest possible figure for a two-hour search, $39.20, rounded off to $40.

Under the amendments, the Secretary will consider all "public interest" waiver requests under the six factors outlined in the DOJ Memorandum (§ 1015.9(f) (iv) and (v)). Public Citizen commented that the advice in the DOJ Memorandum is inconsistent with the Reform Act, disingenuous, and biased. However, the Commission does not plan to rely on the Justice Department's advice any more or less than it would rely on the legislative history of the Reform Act and its own interpretation of the Act, should a question arise about applicability of the "public interest" waiver. The six factors merely isolate and restate the statutory language, and the Commission finds them to be a useful framework for its regulation. Therefore, they are retained in the final amendments.

The Secretary's decisions on waivers will be appealable to the General Counsel (§ 1015.9(f)(vi)).

9. Other amendments concerning the assessment and collection of fees follow the OMB Guidelines:

(a) The Commission will assess interest charges on an unpaid bill, starting on the 31st day after the billing was sent (§ 1015.9(g)(i)).

(b) The Commission will assess charges for time spent searching, even if responsive documents are not located or located documents are exempt from disclosure (§ 1015.9(g)(ii)). Such charges shall not exceed $25, unless the requester has authorized a higher amount.

(c) The Commission will require advancce payment if (1) charges are estimated to exceed $250 and the requester has no history of payment and cannot provide satisfactory assurance of payment, or if (2) a requester has previously failed to pay within 30 days of the billing date (§ 1015.9(g)(iii)).

(d) The Commission will aggregate requests for billing purposes when it reasonably believes that one request has been "broken down" into a series of requests for the purpose of evading fees (§ 1015.9(g)(iv)).

(e) Under the Reform Act, agencies are prohibitied from charging a fee if the cost of collecting the fee would be equal to or greater than the fee itself. Therefore, the Commission will not charge for any request in which the total bill is less than $9.00 (§ 1015.9(g)(v)), an amount that the Commission estimates is the average cost of proceeding one fee collection.

The amendments will become effective on September 4, 1987. In proposing them, the Commission found that neither an environmental assessment nor an environmental impact statement was required. In addition, because any changes in the numbers of firms affected or the amounts of fees collected under the FOIA are not expected to be substantial, the Commission certified that the proposed amendments were not expected to have a significant economic impact on a substantial number of small entities, under the Regulatory Flexibility Act. 5U.S.C. 603(3).

List of Subjects in 16 CFR Part 1015

Freedom of information.

Pursuant to 5 U.S.C. 552(a)(4)(A), as amended, the Commission hereby amends 16 CFR Part 1015 as follows:

PART 1015—[AMENDED]

1. The authority citation for Part 1015 continues to read as follows:

Authority: 86 Stat. 1207; (15 U.S.C. 2051), 74 Stat. 372 as amended; (15 U.S.C. 1261), 84 Stat. 1670; (15 U.S.C. 1471), 70 Stat. 953; (15 U.S.C. 1211), 68 Stat. 11 as amended; (15 U.S.C. 1191), 81 Stat. 54 as amended (5 U.S.C. 552).

2. Section 1015.9 is revised to read as follows:

§ 1015.9 Fees for production of records.

(a) The Commission will provide, at no charge, certain routine information. For other Commission responses to information requests, the Secretary shall determine and levy fees for duplication, search, review, and other services, in accordance with this section.

(b) Fees shall be paid by check or money order, payable to the Treasury of the United States and sent to the Commission.

(c) The following definitions shall apply under this section:

(1) "Direct costs" means those expenditures which an agency actually incurs in searching for and duplicating (and in the case of commercial requesters, reviewing) documents to respond to a FOIA request.

(2) "Search" includes all time spent looking for material that is responsive to a request, including page-by-page or line-by-line identification of material within documents.

(3) "Duplication" refers to the process of making a copy of a document necessary to respond to a FOIA request.

(4) "Review" refers to the process of examining documents located in response to a commercial use request to determine whether any portion of any document located is permitted to be withheld.

(5) "Commercial use request" refers to a request that seeks information for a use or purpose that furthers commercial, trade, or profit interests.

(6) "Educational institution" refers to an entity organized and operated exclusively for educational purposes, whose purpose is scholarly.

(7) "Non-commercial scientific institution" refers to an entity organized and operated exclusively for the purpose of conducting scientific research, the results of which are not intended to promote any particular product or industry.

(8) "Representative of the news media" refers to any person or organization which regularly publishes or disseminates news to the public, in print or electronically.

(d) A commercial use request may incur charges for duplication, search, and review. The following requests may incur charges only for duplication: A request from an educational institution for records not sought for commercial use; a request from a non-commercial scientific institution for records not sought for commercial use; a request from a representative of the news media. Any other request may incur charges for duplication and search.

(e) The following fee schedule will apply:

(1) Copies of documents reproduced on a standard photocopying machine: $0.10 per page.

(2) File searches conducted by clerical personnel: $3.00 for each one-quarter hour (a fraction thereof to be counted as one-quarter hour). Any special costs of sending records from field locations to headquarters for review will be included in search fees, billed at the clerical personnel rate.

(3) File searches conducted by non-clerical or professional or managerial personnel: $4.90 for each one-quarter hour (a fraction thereof to be counted as one-quarter hour).

(4) Review of records: $4.90 for each one-quarter hour (a fraction thereof to be counted as one-quarter hour).

(5) Computerized records: for central processing, $0.32 per second of central processing unit (CPU) time; for printer, $10.00 per 1,000 lines; and for computer magnetic tapes or discs, direct costs.

(6) Postage: Direct-cost basis for mailing requested materials, if the requester wants special handling or if the volume or dimensions of the materials requires special handling.

(7) Microfiche: $0.35 for each frame.

(8) Other charges for materials requiring special reproducing or handling, such as photographs, slides, blueprints, video and audio tape recordings, or other unusual materials: direct-cost basis.

(9) Any other service: An appropriate fee established by the Secretary, based on direct costs.

(f) Fees shall be waived as follows:

(1) No automatic fee waiver shall apply to commercial use requests.

(2) The first $10.00 of duplication costs shall be waived for requests from educational institutions, non-commercial scientific institutions, and representatives of the news media.

(3) For all other requests, the first $10.00 of duplication costs and the first $40 of search costs shall be waived.

(4) The Secretary shall waive or reduce fees whenever disclosure of the requested information is in the public interest because it is likely to contribute significantly to public understanding of the operations or activities of the government and disclosure of the requested information is not primarily in the commercial interest of the requester.

(5) In making a determination under paragraph (f)(4) of this section, the Secretary shall consider the following factors:

(i) The subject of the request: Whether the subject of the requested records concerns the operations or activities of the government.

(ii) The informative value of the information to be disclosed: Whether the disclosure is likely to contribute to an understanding of government operations or activities.

(iii) The contribution to an understanding of the subject by the general public likely to result from disclosure: Whether disclosure of the requested information will contribute to public understanding.

(iv) The significance of the contribution to public understanding: Whether the disclosure is likely to contribute significantly to public understanding of government operations or activities.

(v) The existence and magnitude of a commercial interest: Whether the requester has a commercial interest that would be furthered by the requested disclosure; and, if so

(vi) The primary interest in disclosure: Whether the magnitude of the identified commercial interest of the requester is sufficiently large, in comparison with the public interest in disclosure, that disclosure is primarily in the commercial interest of the requester.

(6) Any determination made by the Secretary concerning fee waivers may be appealed by the requester to the Commission's General Counsel in the manner described at § 1015.7.

(g) Collection of fees shall be in accordance with the following:

(1) Interest will be charged on amounts billed, starting on the 31st day following the day on which the billing was sent. Interest will be at the rate prescribed in 31 U.S.C. 3717.

(2) Search fees will be imposed (on requesters charged for search time) even if no responsive documents are located or if the search leads to responsive documents that are withheld under an exemption to the Freedom of Information Act. Such fees shall not exceed $25.00, unless the requester has authorized a higher amount.

(3) Before the Commission begins processing a request or discloses any information, it will require advance payment if:

(i) Charges are estimated to exceed $250.00 and the requester has no history of payment and cannot provide satisfactory assurance that payment will be made; or

(ii) A requester failed to pay the Commission for a previous Freedom of Information Act request within 30 days of the billing date.

(4) The Commission will aggregate requests, for the purposes of billing, whenever it reasonably believes that a requester or group of requesters is attempting to separate a request into more than one request for the purpose of evading fees.

(5) If a requester's total bill is less than $9.00, the Commission will not request payment.

Dated: July 23, 1987.

Sadye E. Dunn,

Secretary, Consumer Product Safety Commission.

[FR Doc. 87-17055 Filed 8-4-87; 8:45 am]

BILLING CODE 6355-01-M

COMMODITY FUTURES TRADING COMMISSION

17 CFR Parts 1, 30, 32, and 166

Foreign Futures and Foreign Options Transactions

AGENCY: Commodity Futures Trading Commission.

ACTION: Final rules.

SUMMARY: The Commodity Futures Trading Commission ("Commission") is adopting final regulations governing the domestic offer and sale of options and futures contracts traded on or subject to the rules of a foreign board of trade. These rules are intended to implement the provisions of sections 2(a)(1)(A), 4(b) and 4c of the Commodity Exchange Act ("Act"), which vest the Commission with exclusive jurisdiction over the offer and sale of such instruments in the United States.

EFFECTIVE DATE: January 4, 1988.

FOR FURTHER INFORMATION CONTACT: Jane C. Kang, Esq., Division of Trading and Markets, Commodity Futures Trading Commission, 2033 K Street NW., Washington, DC 20581. Telephone: (202) 254-8955.

SUPPLEMENTARY INFORMATION:

I. Background

On April 8, 1986, the Commission published for public comment a new part 30 to its regulations to govern the domestic offer and sale of futures and options entered into on or subject to the rules of a foreign board of trade. 51 FR 12104.[1] Following an initial comment period of 90 days, the comment period was twice extended and closed on November 14, 1986. Upon careful consideration of all comments received and its own reconsideration of the regulations as proposed in light of its regulatory objectives, the Commission is today publishing final rules.

With the development of international futures markets, and increasing public awareness of such markets, these regulations will add to the Commission's existing customer protection regulatory scheme coverage of foreign futures and options transactions undertaken by U.S. domiciliaries. Throughout the formulation of these rules, the Commission has been guided by Congress' intent that foreign futures and options products sold in the U.S. be subject to regulatory safeguards comparable to those applicable to domestic transactions.[2] In particular, requirements with respect to registration, disclosure, capital adequacy, protection of customer funds and recordkeeping will be applied to the offer and sale of foreign products as they are to the offer and sale of domestic products. In addition, the regulations will extend the open season provisions of section 12(e) of the Act to permit the application of state law to those persons and foreign transactions that operate in violation of the regulatory scheme. Currently, the Commission has exclusive enforcement jurisdiction with respect to all foreign futures and options transactions. *See* section 12(e). Further, the rules potentially are a vehicle for harmonizing regulatory programs among international markets, thus facilitating the growth of these markets.

Finally, the regulations are a prerequisite to permitting the offer and sale of foreign options, now banned, to members of the public.[3] As described in greater detail in section IV, *infra*, pursuant to rule 30.3(a) adopted herein, the Commission intends to authorize by separate order the offer and sale of foreign options on a market-by-market basis.

In order to give affected persons sufficient time to comply with the rules (and to coincide with the effective date of certain offshore regulatory programs), the Commission is delaying their effective date to January 4, 1988. In the interim, the prohibition on foreign options will remain in place, while foreign futures may be offered subject only to the antifraud provisions of section 4b of the Act and current Commission rule 30.02. The Commission is mindful that the implementation of a regulatory scheme such as this is an evolving process, particularly as the issues are numerous and complex. Accordingly, the Commission invites affected persons to seek interpretations of the rules, no-action positions and

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[1] This proposal was preceded by an advance notice of proposed rulemaking that was published in the **Federal Register** on July 25, 1984 in response to amendments to the Act in the Futures Trading Act of 1982, Pub .L. No. 97-444, 96 Stat. 2204, 2299 (1983), 49 FR 29963.

[2] *See* S. Rep. No. 384, 97th Cong., 2d Sess. 45-46 (1982) and 51 FR at 12107.

[3] Although Congress removed the statutory prohibition on the offer and sale of foreign options formerly contained in section 4c(c) of the Act, *see* Futures Trading Act of 1986, Pub. L. No. 99-641, section 102, 100 Stat. 3556 (1987), the regulatory prohibition set forth in Commission rule 32.11, 17 CFR 32.11 (1987), adopted pursuant to section 4c(b) of the Act, remains in effect. This regulatory prohibition, of course, is subject to the trade option exception set forth in Commission rule 32.4, 17 CFR 32.4 (1987).

exemaptions, as appropriate. In this regard, the Commission has determined to retain the general exemptive provision set forth in rule 30.10, as proposed.

As the Commission noted in proposing this rule, among other things, it allows persons located outside the United States that are subject to a comparable regulatory scheme to seek an exemption from the application of certain of the rules adopted herein. In this connection, the Commission is issuing concurrently as Appendix A to Part 30 of these rules, an interpretative statement generally indicating how this exemption would be applied which sets forth the elements the Commission will examine in determining whether to grant an exemption to such persons. As described more completely in the interpretative statement, a party seeking an exemption must set forth with particularity the comparable rule or rules applicable in the jurisdiction in which the party is located. Moreover, any exemption that may be granted will be subject to the condition that the foreign person consensually submit to U.S. jurisdiction by designating an agent for service of process in the United States with respect to the foreign transactions that are the subject of these rules. In addition, the foreign person must agree to make its relevant books and records available in the United States to a Commission or Department of Justice representative.

The Commission would like to make clear that the more general exemption described herein and in the interpretative statement would be available to persons located outside the United States that are subject to a comparable regulatory structure. It is not the Commission's intention to grant such exemptions to persons located in the United States that solicit or accept orders for execution on a foreign board of trade although, as noted above, the Commission will entertain from domestic persons petitions for exemption or no-action to address technical problems of particularity in the application of the Commission's foreign futures and options rules to given persons, as it would with respect to any Commission rules. Otherwise, U.S. persons required to register with the Commission under part 30 generally will be expected to comply in all respects with its provisions and related provisions of the Commission's rules.

II. Summary of Comments on Proposed Rules

During the seven-month comment period, the Commission received thirty letters on the notice of proposed rulemaking, representing five United States contract markets, four futures commission merchants, the Futures Industry Association ("FIA"), National Futures Association ("NFA"), two United States Government agencies (Departments of Commerce and Justice), the North American Securities Administrators Association, Inc. ("NASAA"), a company which provides bookkeeping systems to futures commission merchants and to other commodity clients in London and Hong Kong, and thirteen foreign commenters. The foreign commenters included five foreign exchanges, one of which submitted its views through a comment letter prepared jointly by a United States law firm and a Canadian law firm, and one letter from the Joint Exchanges Committee in London, representing the views of the London Commodity Exchange Ltd., the Metal Market and Exchange Company Ltd., the London International Financial Futures Exchange Ltd., the Grain and Feed Trade Association, the International Petroleum Exchange of London Ltd., and International Commodities Clearing House Ltd. (hereinafter "London Exchanges"), two foreign commodities firms, one of which is also a registered futures commission merchant, and five foreign governmental entities. Two commenters submitted more than one comment letter. [4] A synopsis of the views of the three major groups of commenters, *i.e.*, U.S. exchanges, U.S. futures commission merchants and foreign exchanges, in addition to that of NFA, follows. A more detailed survey of the comments received is outlined in the analysis of the final rules.

The U.S. futures commission merchants generally questioned the need for any regulation whatsoever. However, their specific concerns centered on the separate segregation requirement, which they believed would be expensive to implement and which they contended their current computer systems would not be able to accommodate. The futures commission merchants also expressed reservations about serving as an agent for service of process of all communications under the proposed alternative procedure, fearing that as a result they could be held responsible for the conduct of the foreign entity over which they had no control. The majority of the futures commission merchants also strongly recommended that the definition of "commercial" persons set forth in proposed rule 30.1 be broadened to include institutional users of the commodities markets and financial institutions.

The U.S. contract markets supported the adoption of a regulatory structure but contended that the proposed rules, if not exactly equivalent to the regulation of domestic products, would give a competitive advantage to foreign exchanges. The contract markets expressed particular concern that commercials would be excluded from the definition of a foreign futures and option customer setting a precedent for a trade futures exception and that foreign futures and option customer funds would not be included in a firm's required capital computation. They specifically addressed the issue of parity with respect to foreign and domestic products stating that these exclusions would make the cost of doing business on a foreign exchange less expensive than the cost of doing business in the U.S. and, hence, would have an anticompetitive effect on the U.S. market. They also expressed concern about the increased threat to U.S. customer funds for lack of capital reflecting the risk of foreign positions in the event of the bankruptcy of the futures commission merchant.

The foreign exchanges also asserted the rules were anticompetitive but, conversely, that they discriminated in favor of the U.S. markets. They particularly expressed concern about the registration requirement for firms not located in the U.S. In their view, the alternative procedure in proposed rule 30.5 provided little relief, since it would require the foreign firm to effect transactions through a registered domestic futures commission merchant.[5] However, they strongly supported the exemptive procedure. The foreign exchanges also objected to the disclosure requirement, contending it suggests that trading on a foreign exchange is riskier than trading on a U.S. exchange. Finally, since foreign exchanges permit "upstairs" or over-the-counter trading, the exchanges asked that the rules make clear that such transactions are not prohibited. Conversely, on this matter, the U.S. contract markets requested clarification that section 4(a), which prohibits the offer and sale of all off-exchange futures contracts, would be applicable to off-exchange foreign futures contracts.

NFA commented that U.S. participants in foreign futures and options transactions should be afforded protections substantially similar to those afforded customers whose transactions are executed on domestic

[4] These commenters were the Department of Justice and the Coffee, Sugar & Cocoa Exchange, Inc. In addition, on July 3, 1987, the Joint Exchanges Committee in the United Kingdom submitted a letter on behalf of the London Exchanges, the Bank of England, the Securities and Investments Board, the Association of Futures Brokers and Dealers and the Department of Trade and Industry urging the Commission to adopt final rules governing foreign futures and options transactions as expeditiously as possible.

[5] Notably, the U.S. exchanges criticized the alternative procedure in proposed rule 30.5 as it would provide an intermediate basis for qualifying to do business from offshore without the corresponding agreement of offshore self-regulators to cooperate in enforcing the regulations.

exchanges. In that connection, NFA urged the Commission to promulgate rules governing registration and minimum financial requirements for firms engaged in foreign futures and options transactions, but commented that maximum flexibility would be achieved if the Commission permitted additional requirements in areas such as segregation, recordkeeping, disclosure and sales practices to be imposed through NFA rulemaking. According to NFA, this approach to regulation would be especially appropriate in view of the apparent general trend among foreign govenments to provide for regulation in their jurisdictions through self-regulatory bodies.

III. Final Rules

A. In General

The rules which the Commission is now adopting reflect the Commission's careful evaluation of the comments received and refinement of its regulatory objectives in this rulemaking proceeding. As a result, the regulatory system outlined in the final rules as adopted herein is consistent with that proposed by the Commission in April of last year while refining the proposed rules in three principal respects. These principal revisions to the proposed rules are discussed at length below, followed by a discussion of the other aspects of the final rules. Generally, these revisions reflect the resolution of issues raised for comment in favor of according substantially comparable treatment, insofar as practicable, to foreign and domestic products sold in the U.S., a resolution that effectuates the overall purpose of the rulemaking. As previously noted, however, the Commission is mindful of the particularly complex nature of the issues presented by these rules as well as the regulatory goals embodied herein. In consideration of the foregoing, and to give affected persons sufficient time to comply or to apply for an exemption through the exemptive procedure in rule 30.10, the Commission is delaying the effective date of the rules to January 4, 1988, and reiterates its invitation to affected persons to seek interpretations, clarifications and exemptions, as appropriate.[6]

B. Principal Revisions to Proposed Rules

Commercial exclusion. Unlike the broad definition of a "customer" for purposes of domestic exchange transactions, the Commission proposed to exclude from the definition of a "foreign futures or foreign options customer" a "producer, processor, or commercial user of, or a merchant handling, the commodity which is the subject of the foreign futures contract or foreign options transaction, or the products or byproducts thereof, when such foreign futures contracts or foreign options transactions are entered into solely for purposes related to its business as such." Proposed § 30.1(c). The Commission, which modeled this exception on the trade option exception, proposed this exclusion based upon the current nonregulation of foreign futures generally and its belief that, historically, persons who had determined to use transactions on foreign exchanges in connection with their business had taken the time to investigate those markets and the brokers with which they would be dealing. As a result, except for the prohibitions on fraud that in any event are applicable to the offer and sale of all transactions on foreign exchanges, the Commission preliminarily determined that such persons may not require the special protections afforded by the Commission's proposed regulatory scheme for the domestic offer and sale of such foreign products. However, the Commission specifically requested comment on whether this exclusion was appropriate.[7]

The commercial exclusion generated strong opinions on both sides of the issue. The exchanges expressed great concern with the Commission's plan to exclude from the definition of "customer" all "commercial" entities, commenting that the proposal is inconsistent with the objectives of customer protection and fair competition. Noting the Commission's statement in the proposal that commercial traders are more sophisticated than non-commercial traders and, therefore, do not need the "special protections" provided by Commission regulations, they commented that the need for such protections is even less compelling when transactions occur on domestic exchanges, where safeguards that may not be found on foreign markets are enforced directly by the contract markets and their clearing organizations, subject to Commission oversight. However, the primary reason the exchanges opposed this exclusion was their concern that it provided a competitive advantage to foreign markets at the expense of domestic markets. Another U.S. commenter noted the Commission's assessment in the proposed rules that virtually all foreign futures and foreign options transactions originating from the U.S. are for commercial accounts and was troubled that the exclusion of commercials from the definition of a foreign futures or foreign options customer would have eliminated the desirable aspects of the Commission's customer protection rules.

The futures commission merchants and foreign commenters who remarked on this provision endorsed the Commission's effort to exempt from the scope of the proposed regulations certain commercial entities. Nevertheless, they believed that the language of the commercial customer exclusion, set forth in proposed rule 30.1(c), should be broadened in two respects. First, the exclusion should be expanded to include a sophisticated professional and business user of the markets who would not strictly be "a producer, processor or commercial user of, or a merchant handling the commodity which is the subject of the foreign futures contract or foreign options transactions. . . ." Second, they suggested that the restriction that an excluded customer enter into the foreign futures or options transaction "solely for purposes related to its business as such" is too narrow and could undermine completely the benefits of the proposed exemption. In this connection, certain futures commission merchants noted that the narrow scope of the exclusion would require them to carry commercials in two separate accounts, since commercials frequently engage in transactions that would not qualify for an exclusion. Hence, the benefits intended by the proposed rule would be lost and administrative problems and costs of doing a global business would be materially magnified. In essence, these commenters endorsed a "sophisticated investor" exclusion from the definition of a foreign futures and foreign options customer.

The Commission finds merit in the position of the U.S. exchanges that "commercials" be included in the definition of a foreign futures and foreign options customer. This assessment is generally consistent with Congressional intent that the Commission adopt rules to protect *all* U.S. residents and that any regulations adopted not result in either domestic or foreign products having a comparative

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[6] The Commission wishes to note that the staff will continue to consider requests for issuance of no-action letters with respect to the offer and sale of foreign futures contracts which are based on stock indices in light of the criteria set forth in section 2(a)(1)(B) of the Act. The rules herein will regulate the offer and sale of foreign futures contracts based on such indices, but does not eliminate the necessity of complying with other provisions of the Act applicable to such contracts.

[7] 51 FR at 12107.

advantage over the other.[8] Moreover, the Commission has determined that it would not be appropriate to expand the scope of the language in the trade option exception to all commercials trading in foreign futures and foreign options. As noted by one U.S. exchange, the mere fact that a firm deals in the underlying commodity does not mean that it is a "sophisticated" trader of all foreign futures or foreign options and that it could not benefit from the safeguards applicable to other non-commercial customers. Further in this regard, as noted above, the futures commission merchant community appeared generally dissatisfied with the scope of the exclusion, arguing that it did not provide meaningful relief as proposed. The Commission, however, was concerned that such an exclusion, particularly in that it may provide lesser protections to funds of institutions which invest and carry funds for the general public, may not be in the public interest. Therefore, the Commission has determined not to exclude commercials from the definition of foreign futures and foreign options customers.[9]

Capital requirements. The Commission proposed no changes to Commission rule 1.17 which currently does not require that foreign futures customer funds be taken into account in computing the firm's minimum net capital requirements, although a futures commission merchant is required to take a charge against its capital for undermargined house proprietary accounts or customer futures accounts (including foreign futures accounts) carried by the futures commission merchant. Commission rule 1.17(c)(5) (viii)–(x), 17 CFR 1.17(c)(5) (viii)–(x) (1987). Thus, as proposed, the rules would not have applied the present four percent of segregated fund captial requirement to foreign futures and options with respect to entities currently registered as futures commission merchants. For entities which registered as futures commission merchants and engaged exclusively in foreign futures or option transactions, an adjusted minimum net capital of no less than $50,000 would have been required under Commission rule 1.17(a). An entity which registered as an introducing broker would have been required to maintain an adjusted net capital of at least $20,000 or be guaranteed by a futures commission merchant. Commission rule 1.17 (a), (j), 17 CFR 1.17 (a), (j) (1987). The Commission specifically requested comment, however, on whether this approach to the minimum net capital requirement of futures commission merchants that carry foreign futures or options was appropriate and, in particular, whether it was sufficient in the case of certain foreign markets that do not have explicit margin requirements. 51 FR at 12107–08.

The U.S. exchanges strongly opposed the proposal not to impose the same capital requirements applicable to domestic transactions on foreign futures and foreign options. Specifically, they commented that domestic and foreign contracts carried by a firm must be treated alike in order to provide a meaningful net capital standard to provide the protections generally envisioned by capital against risk to the financial integrity of a firm, particularly in that margin may not always be assessed, and to insure that foreign products do not enjoy a built-in competitive advantage over domestic products. Otherwise, they argued, U.S. firms will favor the sale of foreign futures and options and firm capital will inadequately protect customers who are sold such instruments. Additionally, they urged the Commission to impose a minimum capital requirement on firms engaged exclusively in the domestic offer and sale of foreign futures and options that accurately reflects the risk inherent in the total positions carried by such firms.[10] Finally, the exchanges noted that the growing availability of such instruments in the U.S. creates a real danger that foreign trading losses could cause an otherwise safe and sound domestic firm to fail.

One foreign exchange also questioned the adequacy of the Commission's proposal in this regard and commented that in the jurisdiction in which it is situated, its member firms are required to include all contracts, including foreign futures and options, in calculating their minimum net capital requirement (except for exempt contracts consisting of spreads in the same commodity entered into on the same commodity future exchange, short covered hedge positions and commodity futures contracts held for financial institutions). One futures commission merchant which commented on this issue noted that the Commission's approach to minimum net capital was appropriate.

On this issue as well, the Commission has considered the comments in light of the proposal's intent to ensure, to the degree reasonably possible, the comparable treatment of domestic and foreign products, and the Congressional directive in this regard. The Commission's capital requirement essentially serves three related purposes. First, it ensures that a firm has made a sufficient financial commitment to doing business and that it has an adequate inclination to operate a responsible business. Second, the capital requirement promotes a firm's stability and enhances its ability to perform as an agent to its customers. Finally, and most importantly, the minimum adjusted net capital requirement promotes a firm's financial integrity and coupled with margin, protects against firm insolvencies. As previously discussed, the U.S. exchanges expressed the view that domestic and foreign products must be treated alike in order to ensure a meaningful net capital standard, and further expressed great concern that the failure to account for foreign futures and options in computing the firm's minimum net capital requirement could affect an otherwise safe and sound domestic firm. For these reasons, the Commission believes that, in light of the differences in margin treatment on foreign exchanges and Congressional concern with respect to the comparable treatment of domestic and foreign products, rule 1.17 should be applied to money, securities and property which a futures commission merchant holds for or on behalf of foreign futures and foreign options customers to secure open foreign futures and foreign options positions as well as domestic positions.[11] Specifically, pursuant to

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[8] S. Rep. No. 384, 97th Cong., 2d Sess. 46 (1982).

[9] The Commission notes, however, that, as under current Commission rules and regulations with respect to transactions on U.S. contract markets, a person trading foreign futures and options solely for proprietary accounts will not be required to register as a futures commission merchant, although such a person will remain subject to all other applicable provisions of the Act of the rules, regulations and orders thereunder. See Commission rule 3.10(c), 17 CFR 3.10(c) (1987).

[10] The Commission has recently sent letters to all of the industry self-regulatory organizations, welcoming their efforts to develop and test a risk-based minimum capital requirement as an alternative to certain proposals advanced by the Commission after the default of Volume Investors Corporation in 1985. The Commission stated that it looks forward to receipt of this proposal, which it understands may be submitted to the Commission within the next few months. The Commission further stated that any such proposal would deserve a prompt, yet thorough, examination and comment process, which will permit all interested parties sufficient time to review and assess its potential impact. However, the Commission believes that the continuing work on a general modification of the Commission's capital rules, however timely, should not further defer the adoption of the rules herein.

[11] The definition of such funds, the secured amount, describes the minimum amount required to be maintained in the separate account or accounts mandated by new rule 30.7 on behalf of foreign futures and options customers. The secured amount can be deposited in an account together with nonregulated customer funds provided there is no competing security interest in such account and the provisions of § 30.7(b) are met.

amendments to rule 1.17, the capital requirement applicable to firms carrying foreign futures and foreign options positions will include four percent of the foreign futures and foreign options secured amount, which is defined in new rule 1.3(rr) and discussed more fully below. The Commission believes this determination is more consistent with Congressional intent and the Commission's goal of ensuring to the extent possible, the parallel treatment of domestic and foreign futures and options products and the financial integrity of firms doing an integrated business.

To effectuate this new determination, conforming amendments have been added to part 1 of the Commission's rules. As referenced above, the definition of foreign futures and foreign options customer funds in proposed § 30.1(d) has been deleted and the definition of foreign futures and foreign options secured amount has been added at rule 1.3(rr) because of the reference to such term in conforming amendments to rules 1.10, 1.16 and, most significantly, in rules 1.12 and 1.17, CFR 1.10, 1.12, 1.16 and 1.17 (1978). This secured amount was adopted in lieu of a separate segregation requirement for excess margin in order to reduce the accounting and transmission problems affiliated with the requirement that all such excess funds be accounted for and maintained onshore. In essence, the foreign futures and foreign options secured amount is an amount equal to the money, securities and property held by, or held for or on behalf of, a futures commission merchant from, for, or on behalf of foreign futures or foreign options customers required to margin, guarantee or secure *open* foreign futures contracts or representing premiums paid or received, plus other funds required to guarantee or secure open option transactions, plus any unrealized gain or minus any unrealized loss on such transactions. In the case of certain foreign options, the Commission understands that premiums paid by customers are held not by the firm but transferred directly to the opposite party to the foreign option contract. Since such premium would not be held by or held on behalf of the futures commission merchant, such premium would not constitute foreign futures and foreign options secured amount.

This will also be the amount to which the existing four percent capital requirement is applied and in calculating the early warning level for firm capital pursuant to 1.12(b)(2) and the firm's adjusted net capital in sections 1 17(a)(1)(i)(B), (b)(2), (c)(5)(iii), (e)(1)(ii), (h)(2)(iv)(C)(2), (h)(2)(vii)(A)(2), (h)(2)(vii)(B)(2), (h)(2)(viii)(A)(2), (h)(3)(ii)(B) and (h)(3)(v)(B) of the Commission's rules. Further, pursuant to amendments to rule 1.10, futures commission merchants must account for money, securities and property received from foreign futures and foreign options customers on the Form 1–FR. Similarly, in rule 1.16, which deals with the qualifications and reports of accountants, paragraph (a)(4) which defines "customer" has been revised to include a foreign futures and foreign options customer as that term is defined in rule 30.1(c).

Foreign Futures and Foreign Options Secured Amounts. In specifying which of the Commission's existing rules and regulations would not be applicable, the Commission noted that rule 1.20, requiring the segregation of customer funds, would not be applicable in recognition of the fact that the Commission could not impose upon members of foreign exchanges, or the foreign exchanges, or the foreign exchanges themselves, the same obligations imposed upon U.S. clearing member firms and clearing organizations consistent with Congressional directive discussed more fully below.[12] Therefore, the Commission originally proposed a separate segregation rule to govern the treatment of foreign futures or foreign options customer funds, imposing upon futures commission merchants carrying foreign futures or options customer funds virtually the same obligations with respect to funds in their possession as they have with respect to U.S. futures or option customer funds as long as such funds are held in the United States. Proposed § 30.7. This rule, in effect, required excess margin funds for foreign transactions to be retained onshore.

Under the modified segregation proposal, futures commission merchants were required to deposit foreign futures or options customer funds in a bank located in the United States [13] or with another futures commission merchant and separately account for and segregate such funds as belonging to foreign futures or option customers. However, such funds subsequently could be deposited with a member of a foreign exchange, with the clearing organization of such foreign exchange or with their respective designated depositories to purchase, margin, guarantee, secure, transfer, adjust or settle foreign futures contracts or options of behalf of the foreign futures or options customer. The requirement of a U.S. deposit before the transmission of funds offshore was intended to insure the availability of bank and futures commission merchant records with respect to such funds which would help establish that they had indeed been transferred on behalf of customers and assist in the tracing of funds.

Proposed rule 30.7 also provided that such funds could, for convenience, be commingled with the funds of other foreign futures or options customers and deposited in the same account or accounts with a bank or trust company located in the United States or with another futures commission merchant, but under no circumstances could such funds be commingled with customer funds required to be segregated under section 4d of the Act and Commission rule 1.20. The Commission expressed concern that to permit such commingling would possibly dilute the pool of funds available to U.S. futures customers in the event of a bankruptcy of the futures commission merchant to the extent funds located overseas could not be repatriated. The Commission's bankruptcy rules provide that for purposes of determining the pro rata distribution of property to customers who hold claims against a debtor, all property segregated on behalf of, or otherwise traceable to, a particular account class is to be allocated to that particular class. Commission rule 190.08(c)(1), 17 CFR 190.08(c)(1) (1987). Thus, to the extent funds located overseas could not be repatriated, if foreign futures and foreign options customer funds were commingled with customer funds required to be segregated pursuant to section 4d, the shortfall in foreign futures and foreign options customer funds would have diminished the pro rata distribution to all customers, including customers trading on domestic exchanges.

However, by requiring foreign futures and foreign options customer funds to be segregated in a separate account, proposed rule 30.7, in conjunction with the Commission's recordkeeping requirements, would have permitted these separately segregated funds to be traceable to a foreign futures or options account class. Provided foreign futures and options customer funds were on deposit in the United States or were otherwise recoverable, foreign futures or options customers would have received the same priority with respect to their

[12] 51 FR at 12108 and proposed § 30.2.

[13] In this connection, the Commission wishes to emphasize that this is a current requirement for domestic futures commission merchants and that a United States branch of a foreign bank may be an acceptable depository.

See Commodity Exchange Authority Administrative Determination No. 238 (September 4, 1974).

funds as U.S. futures and options customers. The Commission also requested comment on whether, in the alternative, this segregation requirement should be eliminated and foreign futures and foreign options customer funds continue to receive a lower priority as was then accorded to them as unregulated funds under the Commission's backruptcy rules.

One U.S. exchange argued very strongly that the Commission should impose identical segregation requirements for funds securing foreign and domestic positions, commenting that the practical effect of the Commission's present proposal is to mislead such customers as to the fate of their funds in a bankruptcy.[14]

On different grounds, U.S. futures commission merchants also objected to the Commission's proposed separate segregation requirement. Essentially, the futures commission merchants noted that the proposed requirement would be extremely complex and costly to implement, requiring major systems changes over an extended period of time. The futures commission merchants noted that in order to comply with the existing segregation requirements of section 4d of the Act, they currently separate customer and non-customer funds. They contended that the Commission's segregation proposal would require the creation of two additional categories within the customer level (commercial and speculative) and could also result in one client being classified in both categories depending upon the commodity being traded. In addition, they commented that separate segregated accounts would be necessary for each possible foreign currency. They contended current systems are not equipped and could not be equipped without excessive cost to handle an additional set of segregated accounts for yen, HK Dollars, Swiss francs, deutschmarks, pounds sterling and Australian Dollars, among other foreign currencies.[15]

They further noted that even if separate segregation could be accomplished without costly systems changes, reporting to clients with respect to such accounts would be confusing and perhaps misleading. Firms also would need to account for segregated (in U.S.) and no longer segregated customer funds (funds transferred to the foreign country) and this would be extremely complex. They were also concerned how to identify accurately where excess funds could be deposited in light of likely substantial nonregulated spot transactions in foreign currencies of their foreign futures and options customers.

One futures commission merchant took a contrary position and commented that it would prefer that no distinction be made between the customer funds of U.S. residents trading in domestic futures and options and the funds of those U.S. residents trading on foreign boards of trade and that these funds be allowed to be retained by futures commission merchants in a consolidated account as long as the funds are located in the United States.[16] If the purpose of the contemplated segregation regulation was to protect the funds of U.S. residents trading in foreign futures and options, this futures commission merchant believed that there was no conceptual basis for treating foreign futures and options customers any differently from U.S. residents who trade on U.S. exchanges or for treating the funds of commercial or institutional customers any differently from those of speculative customers generally. Accordingly, the futures commission merchant requested that consideration be given to the proposition that all U.S. resident customers funds be generally commingled, regardless of the location of the exchange. Finally, this futures commission merchant urged the Commission to clearly authorize futures commission merchants to invest foreign futures and options customer funds in the same manner as they may invest domestic futures and options customer funds.

The majority of the foreign commenters supported the Commission's proposal not to require the segregation in the U.S. of funds necessary to margin foreign futures and foreign options positions overseas, commenting that once foreign futures and option customer funds are transmitted to their respective jurisdictions, such funds are protected by the segregation and other customer protection rules in place in such jurisdictions.

Upon further reflection on this matter, the Commission has determined to modify rule 30.7 to reflect the concerns of the commenters. In so doing, the Commission reaffirms its view that domestic customers of all commodity futures and options products, wherever they originate, should receive substantially the same protections. The Commission further recognizes the inherent limitations on its ability to provide U.S. residents trading on foreign exchanges the identical protections available to U.S. residents trading on U.S. contract markets. Weighed against these considerations, however, is the decision not to promulgate rules which in any way would diminish the pool of funds available to domestic customers trading on U.S. exchanges in the event of a firm failure and not to create biases in favor of the trading of foreign products. Accordingly, pursuant to paragraph (a) of rule 30.7 as adopted, the Commission will require futures commission merchants to maintain in a *separate* account or accounts at least that amount of money, securities and property defined in new rule 1.3(rr) adopted herein, discussed above, which is equal to original client margins set by the futures commission merchant plus accruals and less losses. This amount, "the secured amount," must be deposited in an account accessible on behalf of customers. This rule specifies only the minimum amount required to be maintained in such an account(s). Nothing in these rules prohibits a firm from maintaining additional money, securities and property received from the appropriate customers in such separate account or accounts provided that these amounts are not subject to a competing security interest or claim for noncustomers.

For example, pursuant to new paragraph (b) of this section, the secured amount may, if permitted under foreign laws, be deposited in the same account as are the funds of foreign customers of the futures commission merchant trading on foreign boards of trade

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[14] Another U.S. exchange expressed concern that proposed section 30.7 did not address whether, in linked transactions, it would be permissible for funds received from customers to margin *either* the domestic or foreign positions to be commingled in the same segregated account at the registrant, at a depository, or at the clearinghouse. In that connection, on November 17, 1986, the Division of Trading and Markets issued an interpretative letter at the request of COMEX on the permissible treatment of funds received to margin transactions executed pursuant to COMEX's linkage agreement with the Sydney Futures Exchange. Specifically, the Division stated therein that trades executed on the Sydney Futures Exchange and cleared under the linkage agreement with the COMEX would not be treated as foreign futures but rather as contracts for future delivery on or subject to the rules of a contract market to which the provisions with respect to the segregation of customer funds under section 4d(2) of the Act apply. However, any trades executed on the Sydney Futures Exchange outside of the agreement would be treated as foreign futures. Interpretative Letter No. 86–26, 2 Comm. Fut. L. Rep. (CCH) ¶23,359 (Nov. 17, 1986). *See also* Mutual Offset System's Customer Funds Treatment, Interpretative Letter No. 84–19 [1984–1986 Transfer Binder], Comm. Fut. L. Rep. (CCH) ¶22,389, (Aug. 9, 1984).

[15] In this connection, the Commission notes that a separate account for each foreign currency would not be necessary if such foreign currencies are converted into U.S. dollars.

[16] Under such a system, all foreign futures and foreign options, including funds required to be segregated pursuant to 4d of the Act, would be automatically included in computing the firm's net capital requirement.

provided that the claims of such customers do not diminish the amount required to be on deposit by rule 30.7.[17] Consequently, new paragraph (b) to rule 30.7 requires that, in such instances, the amount on deposit in such account or accounts may be no less than the greater of: (i) The foreign futures and foreign options secured amount plus the amount required to be on deposit if all such customers were foreign futures or foreign options customers under part 30; or (ii) the foreign futures or foreign options secured amount plus the amount required to be held in such separate account(s) for or on behalf of customers pursuant to any law or rule, regulation or order thereunder, or any rule of any self-regulatory organization authorized thereunder, in the jurisdiction in which the depository or the customer is located. This is because, if these funds are subject to an offshore segregation requirement, it is not clear that the priority on behalf of domestic foreign futures and options customers would prevail, as the funds would constitute a trust for two purposes. In the case of other excess funds permitted to be maintained in the separate account, of course, foreign futures and options customers should have a priority claim in the event of insolvency. The foreign futures and foreign options secured amount may not be deposited with money, securities or property of the futures commission merchant or of noncustomers, nor used to secure or guarantee the obligations of such futures commission merchant or of noncustomers. Further, pursuant to paragraph (d), under no circumstances may such secured amount be commingled with funds required to be segregated pursuant to section 4d of the Act and the regulations thereunder.

Pursuant to paragraph (c), the secured amount must be deposited in a separate account or accounts maintained under an account name clearly identifying them as such with a bank or trust company located in the U.S. or as designated, another futures commission merchant, the clearing organization of any foreign board of trade, any member of such foreign board of trade or their designated depositories as permitted under applicable local law. Also pursuant to paragraph (c), as with funds required to be segregated pursuant to section 4d, futures commission merchants must retain in their files for the period designated in rule 1.31, an acknowledgment from the depository that it has been advised that the money, securities or property are held for or on behalf of foreign futures and foreign options customers and are being held in accordance with the provisions of these regulations.

This permits futures commission merchants to continue to document other money, securities and property belonging to foreign futures and foreign options customers deposited in respect of nonregulated transactions such as spot currency transactions subject only to certain recordkeeping and reporting requirements. These requirements include, but are not limited to, the provisions of rule 1.10(d), which, in essence, requires futures commission merchants to include such unregulated funds in addition to the foreign futures and options "secured amount" in completing the Form 1–FR; the requirements of new paragraph (e) to § 30.7, which parallels Commission rule 1.27(a), 17 CFR 1.27(a) (1987), and requires futures commission merchants to account strictly for the investment of money, securities or property on behalf of foreign futures or foreign options customers; new paragraph (f), which parallels Commission rule 1.32, 17 CFR 1.32 (1987), which requires a daily calculation of all funds on deposit, the total amount of money securities and property required to be on deposit in such separate account(s) and, finally, the amount of the futures commission merchant's residual interest in such funds.

In this connection, the Commission's bankruptcy rules as noted above and in the preamble to the proposed rules provide that for purposes of determining the pro rata distribution of property to customers who hold claims against a debtor, all property segregated on behalf of, or otherwise traceable to, a particular account class is to be allocated to that particular class. Commission rule 190.08(c)(2), 17 CFR 190.8(c)(2) (1987). Under such a formulation, therefore, the Commission does not need to amend its bankruptcy rules. Foreign futures and options secured amounts would be automatically allocated to foreign futures and options customers, to the extent such funds are on deposit in the U.S. or are repatriated. In addition, by imposing strict recordkeeping requirements set forth in rule 30.7(d) and other applicable Commission rules, all money, securities and property held for or on behalf of foreign futures and foreign options customers, should also be traceable to such foreign futures and foreign options account class. Provided these funds are on deposit in the U.S. or may be recovered, such customers should receive such funds on a pro-rated basis.

C. Other Final Rules

Definitions. The proposed rules set forth definitions of, among other terms, "foreign futures" and "foreign options". Proposed § 30.1. These definitions were drawn from similar definitions relating to domestic exchange-traded futures and options. Thus, the definition of "foreign options" paralleled the definition of "commodity option" at Commission rule 1.3(hh), 17 CFR 1.3(hh) (1987). Similarly, the term "foreign futures" was drawn from the definition of the same term at section 761(11) of the Bankruptcy Code, which previously had been incorporated by reference in the Commission's own bankruptcy rules. *See* Commission rule 190.01(t), 17 CFR 190.01(t) (1987). The term "foreign futures", therefore, was defined to include a "contract for the purchase or sale of any commodity for future delivery made, or to be made, on or subject to the rules of any board of trade located outside the United States, its territories or possessions." [18] The Commission specifically requested comment on whether the terms "foreign futures" and "foreign options" may be defined more precisely.

One exchange commented that the Commission's proposed definition of foreign futures was unnecessarily restricted to contracts traded on a "board of trade." It suggested that the Commission adopt the statutory formulation—"board of trade, exchange, or market"—in the definition to ensure that the regulatory scheme will be applicable to all forms of futures and options contracts executed in a foreign location.

One futures commission merchant noted, however, that read in conjunction with proposed rule 30.3, the definition of foreign futures in rule 30.1 would prohibit all off-exchange foreign futures transactions, regardless of the fact that a particular transaction may be entirely consistent with the laws or organized trading practices of the foreign nation. Noting that there are significant "curb" markets that should not be embraced in such a definition, it urged the Commission to amend the definition by adding at the end of that subsection

[17] Specifically, if a firm has foreign futures and foreign options customers as well as clients overseas who trade on foreign boards of trade, the funds of all such customers may be consolidated in the same account or accounts.

[18] A "board of trade" is defined at section 2(a)(1)A) of the Act and §1.3(a), 17 CFR 1.3(a) (1987), of the Commission's rules to include "any exchange or association, whether incorporated or unincorporated, of persons who shall be engaged in the business of buying or selling any commodity or receiving the same for sale on consignment."

". . . or otherwise consistent with the laws of any other nation."

First, the Commission notes that it did not intend in any way to limit the definition of foreign futures subject to coverage under these regulations, and subject to the other limitations of the Act, by abbreviating the statutory term, "board of trade, exchange, or market" to simply "board of trade." In that connection, this problem has been ameliorated by the addition of the definition of "foreign board of trade" at rule 1.3(ss) in part 1 of the Commission's rules to mean "any board of trade, exchange or market located outside the United States, its territories or possessions, whether incorporated or unincorporated, where foreign futures or foreign options transactions are entered into."

With respect to the concern expressed by the futures commission merchant that the definition of "foreign futures" would prohibit all off-exchange foreign futures transactions, including transactions deemed lawful in the jurisdiction in which they occur, the Commission has already taken note of the fact that not all foreign commodity exchanges may operate in the same manner as domestic exchanges and that questions may arise as to whether a particular transaction either is, or should be, a foreign futures or foreign option. The Commission also takes note of legislative history in this regard in which Congress stated that in adopting rules in this regard, the Commission should "take into account the customs and practices of foreign boards of trades or markets and recognize that differences may exist between the practices of foreign boards of trade and their U.S. counterparts." [19]

The Commission reiterates its belief that these terms should be interpreted as broadly as possible in order to effectuate the intent of Congress. As the Commission previously commented in the proposed rules, the London Metals Exchange ("LME") is often referred to as a principals' spot and forward market rather than a futures market; however, to the extent the members of the LME execute transactions for futures delivery for or on behalf of U.S customers, such transactions by the Commission would be deemed to be foreign futures transactions for purposes of part 30. At the same time, the Commission also emphasized that these rules do not permit the offer and sale in the U.S. of futures and options which are not executed *on or subject to* the rules of a foreign board of trade and that, pursuant to the terms of section 4(a) of the Act, the domestic offer and sale of off-exchange futures contracts, whether foreign or domestic, is prohibited.[20] Thus, off-exchange products have already been explicitly prohibited, regardless of whether such transactions may be deemed lawful by the jurisdiction in which they occur.

However, in amending section 4b of the Act in the Futures Trading Act of 1986 to make explicit that the prohibition against fraud applies to the offer and sale of all commodity futures contracts, regardless of where traded, Congress clarified that "antifraud enforcement action brought under 4b involving foreign futures contracts will not be directed at the rules of, or trading practices occurring on, foreign boards of trade, exchanges, or markets, or at the terms or conditions of the futures contracts traded on such boards of trade, exchanges or markets." In that connection, Congress stated that it does not intend that certain activities which occur subject to the rules of foreign markets such as curb trading or after-hours trading be the subject of Commission enforcement action for fraud.[21] To the extent questions arise as to whether a particular transaction occurs subject to the rules of a foreign board of trade, the Commission encourages affected persons to request staff interpretations.

Applicability of the Act and regulations. To effectuate the dual purposes of insuring that domestic customers of all commodity futures and options products wherever they originate receive substantially the same protections against improper sales practices and to limit any additional burden on current Commission registrants as the result of the adoption of a regulatory scheme to affect the marketing by them of these products, the Commission determined not to propose an entirely new regulatory structure. Rather, the Commission proposed that, except as specified or unless the context otherwise requires, the Act and the existing regulations thereunder should be deemed applicable to the persons and transactions subject to the requirements of part 30 as though they were set forth therein. Proposed § 30.2. Consistent with the above, the regulations governing the conduct of Commission registrants, including the Commission's recordkeeping and reporting requirements, would have been applicable to the persons required to be registered in the same capacities under part 30 in connection with the transactions subject to regulation under such part. In paragraph (b), the Commission identified certain specific provisions of the Commission's rules which would not be applicable.

Several foreign commenters expressed the concern that such a blanket provision regarding the applicability of the Act and regulations could lead to misunderstandings about the applicable law, particularly on the part of the foreign entities to whom, among others, the regulations would apply. Accordingly, they urged the Commission to amend the proposed regulations to identify explicitly those statutory provisions and regulations which are intended to apply to foreign futures and foreign options transactions. The Commission finds merit in this comment and, accordingly, has revised rule 30.2 to identify the provisions of the Act and regulations which will generally be applicable to such transactions. Specifically, rule 30.2(a) provides that sections 2(a)(1), 4, 4c, 4f, 4g, 4k, 4l, 4m, 4n, 4o, 4p, 6, 6c, 6d, 8, 8a, 9, 12, 13 and 14 of the Act and parts 1, 3, 4, 10, 11, 12, 13, 14, 21, 155, 166 and 190 of the Commission's regulations will apply, as appropriate. Further, in that regard, in rule 30.2(b), the Commission has expanded upon which of the Commission's rules and regulations, particularly those in part 1 of the Commission's regulations, will not be applicable to the transactions herein. Specifically, the provisions of §§ 1.20 through 1.30, 1.32, 1.35(a) (2-4) and (c)-(i), 1.36(b), 1.38, 1.39, 1.40 through 1.51, 1.53, 1.54, 1.55, 1.58, 1.59, 33.2 through 33.6 and parts 15 through 20 of the Commission's rules shall not be applicable to foreign futures and foreign options transactions.

The Commission also wishes to highlight here several other provisions in part 1 which will be specifically applicable to foreign futures and options transactions as if the terms "foreign futures", "foreign option" and "foreign futures and option customer" appeared therein or because by their terms, they are sufficiently broad to encompass such persons and transactions.[22] These rules include the requirements of rule 1.31, dealing with the books and records required to be maintained under the Act and regulations; rule 1.34, pertaining to the preparation of a monthly "point balance"; rule 1.35 (a), (a-1), (b) (1)-(3), concerning records of cash commodity, future and options transactions; rule 1.36(a), concerning records of securities and property received from futures and

[19] S. Rep. No. 384, 97th Cong., 2d Sess. 46 (1982).

[20] *See* 51 FR at 12106.

[21] S. Rep. No. 291, 99th Cong., 2d Sess. 23-24 (1986).

[22] Other sections of part 1 which will apply have been explicitly incorporated into part 30 as paragraphs (d) and (e) of section 30.7.

option customers; rule 1.37 which requires firms to maintain a record of the customer's name, address and occupation and of the guarantor or controller of the account, if any; rule 1.52, which deals with the adoption by U.S. self-regulatory organizations of surveillance and minimum financial requirements; rule 1.56 which is the prohibition on guarantees against loss; rule 1.57 which deals with the operations and activities of introducing brokers; and rule 1.70, which requires the appropriate state official to notify the Commission of state enforcement actions brought under the Act. Finally, with respect to speculative position limits for foreign futures and foreign options generally, the Commission notes that contract markets, pursuant to the provisions of Commission rule 1.61, or NFA at the direction of the contract markets, may impose such limits with respect to their members if they so wish.

Prohibited transactions. Proposed rule 30.3 generally prohibited the offer and sale in the United States of any foreign futures contract or foreign options transaction except in accordance with the provisions of part 30. Specifically, except for persons not located in the United States that elected the alternative to registration contained in proposed rule 30.5, any person engaged in the domestic offer and sale of foreign futures or options would have been required to register in an appropriate capacity as required under proposed rule 30.4 and to be a member of a registered futures association that had provided for the regulation of the foreign futures and options-related activities of its members in a manner equivalent to that governing the domestic futures and options-related activities of its members. Proposed § 30.3(b). Moreover, except for persons not located in the United States that elected the alternative to registration contained in proposed rule 30.5 and that, in addition, deposited $50,000 with a futures commission merchant, foreign futures or options solicited from a foreign futures or options customer in the United States were required to be carried on a fully-disclosed basis by or through a futures commission merchant. Proposed § 30.3(c). The purpose of proposed rule 30.3(c) was to create a domestic record of foreign futures and options transactions entered into by U.S. customers and to ensure that any funds deposited by a foreign futures or options customer prior to transmission abroad would be deposited with a futures commission merchant subject to the segregation requirements of proposed rule 30.7.

The only foreign futures or options transactions entered into by foreign options or foreign futures customers that would not have been subject to regulation, other than antifraud regulation, under part 30 were those transactions "executed on a board of trade located outside the United States, its territories or possessions, subject to an agreement with a contract market that permits positions in a commodity interest which have been established on one of two markets to be liquidated on the other market",[23] *i.e.*, a link agreement such as that which presently exists between the Chicago Mercantile Exchange and the Singapore International Monetary Exchange ("SIMEX") and the Commodity Exchange, Inc. and the Sydney Futures Exchange.[24] Proposed § 30.3. Since transactions under such link agreements generally are effected pursuant to rules of a contract market located in the U.S. that have been approved by the Commission under section 5a(12) of the Act and rule 1.41, the Commission noted that such transactions are already subject to the panoply of the Commission's regulations, including the requirement that such transactions may be solicited or accepted only by Commission registrants.[25]

Although one U.S. exchange commented that a linkage agreement should not be a means of eluding the regulations proposed to be adopted, the remaining commenters on this issue supported the exclusion for linked transactions on the ground that transactions subject to such agreements are adequately regulated by the Commission and additional regulation would be essentially unnecessary and duplicative.

COMEX noted, however, that the text of the proviso in proposed section 30.3(a) is too narrow in scope. Specifically, the proviso describes only a two-exchange linkage whereas it is foreseeable that linkages will be formed among more than two markets. For example, a linkage might consist of three exchanges, located in the U.S., Asia and Europe, to maximize the benefits of 24-hour trading. Accordingly, COMEX recommended that the text of the proposed section 30.3 be modified to read as follows:

> . . . subject to agreement with and rules of a contract market which permit positions in a commodity interest which has been established on one market to be liquidated on *another* market.

The Commission has taken note of this suggestion and has incorporated appropriate amendments to rule 30.3(a).

The Commission has further added a new proviso to rule 30.3(a), as adopted. Specifically, language has been added to paragraph (a) that notwithstanding any other provisions of part 30, it shall be unlawful for a person to engage in the offer and sale of any foreign options until the Commission, *by order*, authorizes such foreign option to be offered in the U.S. As the Commission noted in its proposal, although the regulations contemplated that the prohibition on foreign options would be lifted, the Commission had not made a final decision to do so. In this connection, the Commission further stated that its decision would rest, in part, on the ability of the Commission to obtain information from the foreign exchange with respect to transactions entered into on that exchange on behalf of U.S. customers.[26] Accordingly, in order to ensure that foreign exchanges are both willing and able to share appropriate information with the Commission, particularly since blocking statutes in many foreign jurisdictions may inhibit such foreign exchange from providing such information, the Commission has determined to make the issuance of a Commission order authorizing the offer of a particular foreign option a prerequisite to the lawful offer and sale of such products. The Commission has determined that, in issuing such an order, the existence of an appropriate information sharing arrangement will be a consideration.[27]

Further, in this regard, the Commission notes that the current options ban applies to transactions executed pursuant to a link agreement and that the rules adopted herein will have no effect on the ability of options to be offered and sold pursuant to such links. The Commission wishes to clarify that it intends to approve the offer and

[23] *See* rule 1.59(a)(5), 17 CFR 1.59(a)(5) (1987).

[24] In an earlier interpretative letter concerning the treatment of customer funds under the Chicago Mercantile Exchange's agreement with SIMEX, the Commission's staff clarified that any trades executed on the SIMEX *outsie* of the agreement would be treated as foreign futures. Interpretative Letter No. 84-19, [1984-1986 Transfer Binder] Comm. Fut. L. Rep. (CCH) ¶ 22,389 (Aug. 9, 1984). *See also* n. 14, *supra*.

[25] *See* 51 FR at 12108.

[26] 51 FR at 12105.

[27] Access to necessary information is essential if the Commission is to fulfill its obligations under the Act with respect to customer protection. For example, the Commission should be able to confirm by a simple telephone call or telex to the appropriate regulatory authority, such as the Securities and Investments Board or, alternatively, the Association of Futures Brokers and Dealers or other relevant self-regulatory organization whether a firm is, in fact, registered.

sale of a particular option traded pursuant to a link agreement by approval of a rule submission in this regard by the appropriate contract market. In considering the submission, the Commission intends to apply the same standards discussed above in connection with the issuance of a Commission order pursuant to rule 30.3(a).

Paragraph (b) of proposed § 30.3 which required each registrant to be a member of a registered futures association that regulates foreign futures and foreign options activities has been deleted. Under the Act and current regulations, NFA is effectively required to regulate the activities of *all* registrants and, therefore, the Commission has concluded that rule 30.3(b) is unnecessary.[28] Accordingly, paragraph (c) of proposed rule 30.3 has been redesignated as paragraph (b). In addition, this paragraph has been amended to clarify that persons located overseas are eligible to request an exemption from the application of this paragraph which makes it unlawful for any person, unless otherwise provided in § 30.4 (which sets forth the registration requirement), to engage in the offer and sale of any foreign futures contract or foreign option other than by or through a futures commission merchant on a fully-disclosed basis. Thus, although, as discussed in more detail below, persons located outside the United States are no longer eligible to act, through the alternative procedure, in the capacity of a futures commission merchant without first registering as such and maintaining an office in this country, they may request an exemption from the application of this rule through rule 30.10. As a result of this change, offshore firms have three choices, as more fully discussed below.

Registration. Except as described in rule 30.5 with respect to persons located outside of the U.S., the Commission proposed to require that persons who act in the capacity of futures commission merchant, an introducing broker, a commodity pool operator or a commodity trading advisor in the United States with respect to foreign futures or options customers register in the appropriate capacity with the Commission.[29] Proposed § 30.4. As Commission registrants, such entities would be subject generally to all of the regulatory requirements which currently apply to each category of registrant.[30] In addition, paragraph (e) as proposed required all persons required to be registered under this section and who did not elect the alternative procedure to maintain an office in the U.S. managed by a person domiciled in the U.S. and registered with the Commission as an associated person.

One U.S. exchange and NFA supported the Commission's regulatory objective of requiring the registration of appropriate persons. Specifically, NFA noted that it supports a registration requirement for persons doing a domestic business in foreign futures and options subject to appropriate exemptions and exclusions. In general, NFA believes that the proposed rules set forth appropriate requirements especially in view of the Commission's expressed willingness to grant exemptions pursuant to proposed rule 30.10 based on foreign regulatory protections and understandings with foreign governments and self-regulatory organizations.

However, one U.S. futures commission merchant and the London Exchanges commented that it was inappropriate to subject foreign entities and their business activities outside the United States to the Commission's rules and regulations. Further, the London Exchanges again expressed the view that the Commission has no authority to regulate the offer and sale of foreign futures contracts by persons not located in the United States.[31] They further commented that the requirements that a person registered as a futures commission merchant with the Commission pursuant to the proposed rules must maintain records and an office in the United States are burdensome, unnecessary, and discriminatory as against foreign brokers. Still another foreign exchange noted the serious consequences of proposed rule 30.4(e) which required all registrants to have a branch office in the U.S.[32] Specifically, it noted that under the U.S. Internal Revenue Code, the location of a branch office in the U.S. which engages in a U.S. trade or business with effectively connected income will subject that office to U.S. taxation.

With one major exception discussed below, the Commission has decided to adopt this section essentially as proposed. In addition to certain technical amendments to rule 30.4, the Commission has exempted from the commodity pool operator registration requirement, any investment trust, syndicate, or similar form of enterprise located outside the United States, its territories or possessions which is registered as an investment company under the Investment Company Act of 1940 and whose securities are registered in accordance with the Securities Act of 1933, or which is exempt from such registration requirements. However, this exemption is only available if no more than 10 percent of the participants in, and the value of the assets of, such investment trust, syndicate or similar form of enterprise located outside the United States, its territories or possessions are held by or on behalf of foreign futures and foreign options customers. §30.4(c). In essence, the Commission has incorporated an "otherwise regulated" exemption standard in this regard subject to a 10 percent limitation on the number of U.S. participants and the aggregate value of ownership by U.S. residents.

The Commission has also amended paragraph (d) to exclude from the definition of the term "commodity trading advisor" an insurance company subject to regulation by any state, or any wholly-owned subsidiary or employee thereof, provided that the furnishing of such trading advisory services is solely incidental to the conduct of its business or profession.[33]

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[28] *See* Commission rule 170.15, 17 CFR 170.15 (1987) and NFA Bylaw 1101. NFA commented that at present, it had not provided for the regulation of the foreign futures and foreign option-related activities of its members and in order to do so, NFA would have to amend its Bylaws to include foreign options and futures within NFA's definition of such products. NFA expects that it would take this step if the Commission adopted registration requirements applicable to foreign futures and foreign options transactions.

[29] In this connection, under rule 30.4 as proposed and adopted, the only persons required to register as a commodity trading advisor are those persons who solicit or manage discretionary accounts in foreign options or foreign futures.

[30] At the time the rules were proposed, the Commission stated that this registration requirement will serve to identify those who are lawfully engaged in the offer and sale of foreign futures and options and, thus, will assist those states that may wish to apply their laws to those who are unlawfully engaged in such activity. 51 FR at 12106.

[31] As the Commission has previously noted, however, nothing in section 4(b) or its legislative history limits the Commission's authority over foreign options and futures in section 2(a)(1)(A) of the Act. *See* 51 FR 12104.

[32] *See* 51 FR at 12109.

[33] This amendment is consistent with recent developments in this area. Specifically, in adopting the Futures Trading Act of 1986, the House Committee on Agriculture declined to adopt a proposed statutory amendment to exclude, among others, a life insurance company subject to regulation by any State from the definition of a commodity trading advisor provided that its commodity advisory activities are solely incidental to its bussiness. However, the Committee urged the Commission to issue regulations in this regard. H.R. Rep. No. 624, 99th Cong., 2d Sess. 46–48 (1986). In that regard, on May 26, 1987, the Commission published in the Federal Register proposed rules which would exclude, among others, the above-described insurance companies from the definition of a commodity trading advisor. 52 FR 19522.

This paragraph has also been amended to specify that registration as a commodity trading advisor will not be required if a person is already registered as, among other things, a commodity pool operator or is otherwise exempt from registration pursuant to rule 30.5.

As noted above, the most significant amendment to this section appears in paragraph (e), which, as proposed, had provided that *any* person required to be registered under this section and who did not elect the alternative procedure for non-domestic persons under proposed rule 30.5 must maintain an office in the U.S. managed by a registered associated person. As adopted, the paragraph now provides that any person required to be registered as a *futures commission merchant* under this part must maintain an office in the United States which is managed by an individual domiciled in the United States and registered with the Commission as an associated person. Specifically, this amendment reflects the Commission's reconsideration of its preliminary determination to include among those able to elect the alternative procedure to registration entities which act in the capacity of a futures commission merchant.

The Commission was particularly concerned that unscrupulous firms would merely establish their base of operations offshore, particularly in a locale which has no history or an inadequate history of cooperation with U.S. regulators and law enforcement officials, and by making the $50,000 deposit, solicit and accept money, securities and property from foreign futures and foreign options customers. The Commission was also concerned that the requirement in rule 30.3(b) that all accounts be carried through a futures commission merchant would be insufficient to adequately protect the funds of U.S. customers if carried on an omnibus basis. Accordingly, because the Commission has a paramount interest in the fitness and financial integrity of those entities which receive customer funds, the Commission has determined to require all entities which act in the capacity of a futures commission merchant to register as such.

Thus, for a firm located outside the U.S. which acts in the capacity of a futures commission merchant, the alternative procedure is no longer available and one of three options remain available to it. First, it can register as a futures commission merchant and open an office in the U.S. managed by an associated person who is also domiciled in the U.S. If it elects not to register, it is restricted to acting in the capacity of an introducing broker with respect to accounts which it solicits and all trades must be carried by a U.S. futures commission merchant on a fully-disclosed basis. As a third alternative, firms located in jurisdictions which, among other things, impose customer protection rules similar to those imposed by the Commission are eligible to seek an exemption from the futures commission merchant registration requirement in rule 30.4(a) through the exemptive procedure in rule 30.10.

Alternative procedures for non-domestic persons. As previously noted, the Commission proposed to exempt from registration any non-domestic person that solicited United States residents to trade foreign futures or options, if the person otherwise qualified to do business by entering into an agreement with a futures commission merchant through which the foreign futures or options that person solicited in the United States are carried,[34] designating that futures commission merchant as the agent for the service of process for communications both from the Commission and from the customers of the non-domestic person. Proposed § 30.5. A non-domestic person that would otherwise be required to be registered as a futures commission merchant and would be exempt from registration under the proposed rule generally would not have been able to accept customer funds except through a registered futures commission merchant on a fully-disclosed basis. However, that person would have been able to carry its foreign futures and foreign options customer accounts with a futures commission merchant on an omnibus basis if it deposited with that futures commission merchant money, securities or property in the amount of $50,000. The Commission specifically requested comment on the adequacy of the proposed alternative registration to protect the public.[35]

One U.S. exchange commented that this alternative to registration should be withdrawn and that all entities engaged in the offer and sale of foreign futures and options to customers in the U.S. should be required to register in the appropriate category or to create a U.S. subsidiary or affiliate. If a foreign entity finds this requirement too burdensome, the exchange commented that the foreign firm should be prohibited from having direct contact with U.S. customers. In the alternative, should the Commission determine to permit this alternative procedure, the exchange urged that the amount of money to be deposited with the futures commission merchant through which the foreign firm conducts business should be strictly related to the scale of foreign futures and foreign options activity with U.S. residents.

The foreign commenters, on the other hand, generally expressed the view that the alternative procedure put foreign market professionals at a clear competitive disadvantage by creating what is, in essence, a "tying arrangement," since the foreign entity's access to U.S. customers would be conditioned on the willingness of a domestic competitor to act as its agent. They argued that this requirement would discourage domestic customers from doing business with foreign brokers since by dealing directly with the U.S. futures commission merchant, the customer could avoid the additional costs of the domestic futures commission merchant's processing costs. The futures commission merchants and NFA supported the alternative procedure but the futures commission merchants expressed concerns about first, the scope of the term "communications" and, second, serving as an agent for service of process of all communications. Specifically, they were concerned that they would be held liable for the entirety of the foreign entity's conduct.

On the first issue of permitting persons located outside the U.S. to utilize the alternative procedure, the Commission, as noted above, has reassessed its initial position in this regard and has determined to exclude futures commission merchants from the class of registrants eligible for this alternative procedure. Accordingly, paragraph (c) of rule 30.5, as proposed, concerning the authority to act as an futures commission merchant has been deleted. Persons located overseas are reminded, however, that they may seek an exemption from this requirement pursuant to § 30.10.

Persons who act in the capacities of the remaining categories of registrant, that is, introducing brokers, commodity pool operators and commodity trading advisors and who are located outside the U.S. continue to be eligible to utilize the alternative procedure.[36] However, the Commission takes special note of the fact that pool operators located outside the U.S. will also be able to

[34] *See* proposed rule 30.3(c).

[35] *See* 51 FR at 12109.

[36] Pursuant to amendments to rule 30.4(c), however, certain foreign commodity pool operators may be exempted from the commodity pool operator registration requirement and, thus, would not be subject to the requirements of rule 30.5.

accept funds, securities or property from foreign futures and foreign options customers and that, as is the case of pools offering domestic products, the Commission is not similarly requiring such persons to have a base of operations in the U.S. In that connection, the Commission notes that pursuant to rule 30.6(b)(1), such persons remain subject to the disclosure requirement in rule 30.6(a)(1) the purpose of which is to alert foreign futures and foreign options customers to certain of the risks associated with such transactions. However, because of the Commission's paramount interest in protecting, to the degree reasonably possible, money, securities and property of all customers, the Commission intends to monitor this area closely. Specifically, if the Commission finds a pattern of abuse by foreign pool operators, the Commission will take appropriate measures to remedy any such problems.

With respect to the two concerns expressed by the futures commission merchants in regard to the alternative procedure, the first, regarding the scope of the term "communications," has been remedied by appropriate amendments to rule 30.5(a) which now reads, in part: "For the purposes of this section, the term communication includes any summons, complaint, order, subpoena, request for information, or notice, as well as any other written document or correspondence relating to any activities of such person *subject to regulation under this part.*"

With respect to the second concern, the futures commission merchants stated that they should not be required to serve as an agent of an exempt person for purposes of receiving all customer communications since customers will have been solicited by and will have been doing business with the exempt entity, not the U.S. futures commission merchant. In this regard, the Commission is concerned that a significant degree of customer protection as well as the Commission's ability to regulate effectively foreign futures and options transactions would be lost if the Commission and the foreign entities' customers do not have a means of communicating with the foreign entity in a timely manner. In addition, as noted by the Commission in adopting rule 15.05, 17 CFR 15.05 (1987), which currently requires the designation of a futures commission merchant or introducing broker to be the agent of a foreign broker, customers of a foreign broker and foreign traders, in the past, the Commission's attempts to communicate *directly* with certain foreign persons have not always been well received, either by the recipient, or the recipient's foreign government.[37] Accordingly, the Commission is of the opinion that the designation of an agent for service of process is a significant element of the Commission's customer protection scheme.[38]

However, the Commission has taken note of the futures commission merchants' concerns and has determined that the same objectives may be achieved by broadening the scope of persons to be among those who are eligible to act as an agent for service of process. Specifically, rule 30.5 has been amended to include a registered futures association, *i.e.*, NFA, or any other person located in the United States in the business of providing such services. It is expected, however, that ordinarily the agent will be a futures commission merchant or the NFA.

Another amendment to rule 30.5 incorporates the comment of one futures commission merchant which suggested that all such agency agreements be filed only with NFA. Accordingly, paragraph (a) has been amended to require that rather than being filed both with the Commission and NFA, such agency agreement must now be filed only with the Vice President-Registration, NFA, with a copy to the Vice President-Compliance, NFA. In addition, NFA has been added, along with other self-regulatory organizations and the Department of Justice as appropriate issuers of communications as is the case with respect to domestic regulations. Conforming amendments in this regard have been added to paragraph (b) dealing with termination of such agreements. In paragraph (c), which identifies the rules applicable to persons exempt from registration under this section, rule 30.7 has been deleted as being applicable since the only entity subject to the requirements of that section, a futures commission merchant, can no longer use the alternative procedure. Finally, in paragraph (d), the Department of Justice has been added as an entity that can require persons exempt from registration pursuant to the alternative procedure to produce the books and records such persons are required to maintain under the Commission's rules and regulations.

Risk disclosure. Under proposed rule 30.6, a futures commission merchant or introducing broker could not open or introduce a foreign futures or options account for a customer without first obtaining written authorization from the customer, which authorization must have included a written risk disclosure statement containing only the language set forth in the proposed rule. The authorization could be contained either in the customer account agreement or on a separate form. However, if the futures commission merchant, introducing broker or an associated person of either had discretionary authority over the customer's account, the futures commission merchant or introducing broker was required to receive from the customer a signed and dated acknowledgment to the effect that he had received and understood the risk disclosure statement. This disclosure was required whether the customer had already been provided with the risk disclosure statement required in rules 1.55 and 33.7 of the Commission's regulations.[39]

Commodity pool operators and commodity trading advisors who direct or guide a customer's commodity interest trading in foreign futures or option contracts were also required to provide customers and prospective customers with the disclosure statement referred to above and receive the required acknowledgment prior to engaging in foreign futures or options transactions on behalf of foreign futures or option customers. The commodity pool operator or commodity trading advisor could make the disclosure language part of the Disclosure Document required by part 4 of the Commission's regulations by inserting it as the only language on the page(s) immediately following the disclosure required to be made by Commission rules 4.21(a)(17) and 4.31(a)(8). Otherwise, a separate disclosure statement was required to be provided. In either case, an acknowledgment was required to be received from such person and maintained in accordance with Commission rule 1.31.

In order to limit any additional regulatory burden that would be placed on Commission registrants, the Commission in proposing the rules determined to adopt, to the extent possible, the language and procedures set forth in NFA's Compliance Rule 2-28, governing disclosure to customers in connection with transactions entered into pursuant to link agreements. The Commission stated that upon receipt of

[37] 45 FR 30426, 30427 (May 8, 1980).

[38] In this connection, as noted earlier, the Commission also intends to make this a requirement for foreign persons granted exemptions from these rules pursuant to rule 30.10.

[39] Under the rule as adopted, the options disclosure statement required under Commission rule 33.7 must also be furnished to a foreign options customer, unless the customer has previously received that disclosure statement in connection with opening a domestic exchange-traded options account under part 33. *See* § 30.6(d).

comments, it expected to coordinate with NFA regarding a uniform disclosure statement with respect to both linked and non-linked foreign futures and options transactions.[40]

One U.S. exchange supported the Commission's risk disclosure proposal, but urged that such disclosure should be required regardless of whether the positions are established in connection with a link. Moreover, the exchange commented that if the Commission adopts a regulatory scheme which provides for different segregation standards offering potentially different consequences in bankruptcy or minimum capital computations which fail to calculate the risk related to foreign futures positions, such matters must receive primary and detailed emphasis in all disclosure documents in standardized language by the Commission.

Conversely, foreign commenters expressed concern that the form of the risk disclosure statement could lead investors to conclude that U.S. contract markets are safer and subject to a greater degree of regulatory oversight and protection and contended that the Commission is inaccurately comparing the relative protections with respect to foreign futures and options contracts versus U.S. products and failing to distinguish between those foreign exchanges which have a history of a customer protection oriented regulatory scheme and those which do not. Instead, they urged the Commission to revise the current risk disclosure statements for U.S. traded futures and options contracts to include an appropriate reference to the market risks of foreign futures and options contracts. Such an incorporation would not only simplify procedures for the futures commission merchant and introducing broker community, but would also render the risks more understandable to the investor, who is already confronted with a myriad of forms and material upon opening a futures or options account.

The futures commission merchants commented that the Commission's decision to coordinate with NFA to achieve a uniform disclosure statement with respect to both linked and non-linked foreign futures and options is appropriate. In that connection, they commented that a separate authorization for foreign transactions should not be required. Rather, they urged the Commission to incorporate the foreign futures and foreign options disclosure statement into the general disclosure documents through amendments to rules 1.55 and 33.7, 17 CFR 1.55, 33.7 (1987). Thus, a maximum of two disclosure documents could be maintained—one for foreign and domestic futures and one for foreign and domestic options. The futures commission merchants further noted that rule 30.6(a)(2) requires a futures commission merchant which has received discretionary authority from a customer to trade foreign futures or foreign options to receive "specific consent" of the customer and a "separate acknowledgment signed and dated by the customer that the customer has received and understood the risk disclosure statement". The futures commission merchants commented that the general power of attorney contained in Commission regulation 166.2 is sufficient authorization for trading of futures and options contracts on all exchanges, domestic and foreign.

Finally, NFA commented that given the increasing integration of international futures and options markets, NFA believes the appropriate goal for NFA and the Commission should be a single risk disclosure statement adequate to apply to instruments traded on domestic, foreign and linked markets. The Commission has taken all of these comments into consideration and has incorporated amendments as it deems appropriate.

First, in response to concerns that the separate consent for such foreign transactions and separate acknowledgment for the risk disclosure statement were unnecessarily burdensome, the Commission has streamlined these requirements. Rule 30.6(a) as adopted, still provides that futures commission merchants and introducing brokers must first deliver the risk disclosure statement to all customers; however, in the final rule, the requirement of a separate customer consent for engaging in foreign futures and options transactions has been deleted. Instead, only those customers who have granted general discretionary authority must expressly authorize such transactions with respect to their account in accordance with the provisions of 166.2. In that regard, rather than requiring a separate authorization, the Commission has amended Commission rule 166.2 to clarify that customers must *expressly* grant in the document the authority to the futures commission merchant and introducing broker to engage in foreign futures and foreign options transactions. The Commission also wishes to clarify that although the futures commission merchant or introducing broker may still receive the separate acknowledgment that the customer has received and understood the risk disclosure statement, this requirement may also be satisfied by incorporating into the text of the customer's grant of general discretionary authority, another acknowledgment, also express, that the customer has received and understood the applicable risk disclosure document.

In addition, the language of the risk disclosure has been revised to incorporate the risks associated with linked transactions. Specifically, the Commission agrees with NFA that a single statement should be used to disclose the risks of trading in foreign futures and options, whether pursuant to a link agreement or not. Accordingly, appropriate language changes have been made in rule 30.6(b). In this connection, the Commission notes that at the option of the futures commission merchant or introducing broker, the disclosure statement in 30.6(b) may be given to linked transaction customers in lieu of that required under NFA Compliance Rule 2-28 or the NFA disclosure may be used. If a firm solicits a customer who engages in both foreign futures and options and linked transactions, the firm's disclosure obligation in this regard will be fulfilled by giving the customer the risk disclosure statement in 30.6(b). If a customer is exclusively a foreign futures and options customer, he must be given the statement in 30.6(b).

Finally, in this regard, the Commission takes note of concerns raised by almost all commenters as to the myriad of disclosure documents required to be provided to customers generally. The Commission has directed its staff, in consultation with NFA, in recognition of its general sales practice responsibility, to review the Commission's disclosure requirements in an effort to explore less burdensome alternatives.

Reporting requirements. In proposed rule 30.8, the Commission proposed to require that futures commission merchants file with the Commission on a monthly basis, separately by foreign exchange and commodity, long and short, customer and proprietary, a report containing data for the total volume of foreign futures contracts effected on such foreign exchange and the open interest at month end. With respect to foreign options, the Commission proposed to require that futures commission merchants report, on a monthly basis, separately by underlying futures contracts for options on futures contracts or by underlying physical for options on physicals, by put, by call, and by customer or proprietary, the total volume and the open interest at month end. The Commission further proposed

[40] 51 FR 12110.

that futures commission merchants report, on a monthly basis, the total amount of foreign futures and foreign options customer funds forwarded to each member of a foreign exchange, a clearing organization of such exchange or their respective designated depositories to purchase, margin or otherwise secure foreign futures or foreign options positions. Further, the Commission requested comment on whether these reports should be filed with NFA rather than with the Commission.

Although one U.S. exchange supported this requirement, many of the other commenters questioned the regulatory purpose of this monthly requirement which many futures commission merchants viewed as being burdensome. As NFA pointed out in its comment letter, however, such information is essential, along with the other reporting and recordkeeping requirements imposed by the Commission, for monitoring compliance with the Commission's financial and other regulatory requirements and targeting certain firms for sales practice audits with respect to their foreign futures and options business. However, the Commission agrees that a monthly requirement may not be necessary and, therefore, has changed the requirement to a quarterly one.[41] The Commission has also deleted subparagraph 5 of paragraph (d) concerning the total amount of foreign futures and foreign options customer funds forwarded overseas as a result of the revisions to the Commission's proposed rules regarding the treatment of such funds. Finally, the Commission is requiring that these reports be filed with NFA rather than the Commission based upon the comment of NFA and a U.S. futures commission merchant that NFA would be the appropriate entity to receive these reports.

Fraudulent transactions prohibited. The Commission proposed to redesignate rule 30.02 as rule 30.9 as modified to reflect the definitions set forth in the part 30 rules. The Commission received only one comment on this proposal, that from a futures commission merchant which had earlier commented on the scope of certain definitions. Specifically, this futures commission merchant noted that the language in 30.9(d) making it unlawful "to bucket any order, or to fill any order by offset . . ." could make certain overseas transactions illegal although such transactions may be ordinary and customary under the rules of a foreign jurisdiction. The Commission reiterates its earlier statement regarding amendments to section 4b of the Act and its comments in this regard.

Exemptive procedure. The Commission notes initially that although persons located in the U.S. may request exemptions in instances of particular hardship from specific requirements set forth in these regulations, the only persons eligible for a broader exemption from the general applicability of the rules are those persons located outside the U.S. who are subject to comparable regulation in the jurisdiction in which they are situated, provided such exemption would not otherwise be contrary to the public interest.

The Commission received many comments on this provision. The U.S. exchanges noted that immediate issues arise as to what constitutes "comparable regulation" and to what extent the enforcement authority in the various foreign nations is equal to the task set forth in statute. Moreover, they commented that the Commission should not accord this sort of recognition to the laws of nations which in many cases do not reciprocate in their treatment of U.S. firms and have obstructed the development of joint surveillance and other reciprocal trading agreements which would facilitate the offer of foreign futures and options by exchanges in this country.[42]

The foreign commenters were generally of the opinion that the exemptive procedure was entirely appropriate. They noted, however, that the Commission should establish an appropriate timetable to permit a substantial grace period between the promulgation of the final rules and their effective date. The grace period should provide sufficient time for an applicant to obtain an exemption or, if the exemption is denied, to obtain registration, should the applicant elect to do so. They further commented that, as a practical matter, the Commission should permit self-regulatory organizations, or government regulators, to apply for exemptions on behalf of all of their members or regulated persons, respectively. This would eliminate unnecessarily repetitious and administratively burdensome applications.

In this regard, the Commission, as previously noted, has delayed the effective date of these rules to January 4, 1988, and, accordingly, more than sufficient time has been provided for interested persons to seek the appropriate exemptions. All of the remaining comments are addressed in Appendix A to the rules herein, which is the Commission's interpretative statement with respect to its exemptive authority under section 30.10.

Applicability of state law. Finally, pursuant to its authority under the "open season" provisions of section 12(e) of the Act, the Commission proposed to authorize the application of any state law to transactions on a foreign exchange entered into by U.S. customers through any person not registered with the Commission or exempt from registration in accordance with this part. In this regard, the North American Securities Administrators Association, Inc. ("NASAA") requested clarification that pursuant to section 12(e)(3) of the Act, the states are not pre-empted from applying their laws against any person required to be registered but who is not so registered. The Commission notes that section 12(e)(3) is already clear in this regard.

In closing, the Commission wishes to make clear that it intends to monitor closely the application of this regulatory scheme for the offer and sale of foreign futures and foreign options in the U.S. and to make adjustments in these rules, as necessary, based, in part, on its experience in administering the exemptive procedure as well as other requests for interpretations of the provisions herein.

IV. Related Matters

A. Paperwork Reduction Act

The Paperwork Reduction Act ("PRA") of 1980, 44 U.S.C. 3501 *et seq.*, imposes certain requirements on federal agencies, including the Commission, in connection with their conducting or sponsoring any collection of information as defined by the PRA. Office of Management and Budget ("OMB") control number 3038–3035 previously has been assigned to these part 30 rules. Other control numbers have been assigned to other rules referred to herein. The Commission previously submitted the propsed rules to OMB. However, the Commission is resubmitting to OMB an explanation and details of the information collection and recordkeeping requirements contained in the final rules. Any person wishing to comment on the information collection requirements should contact Robert Neal, Office of Information and Regulatory Affairs, Office of

[41] Thus, the first such reports would be required on the 10th business day in April 1988.

[42] One exchange further commented because granting such an exemption could have a far-reaching impact, the notice of the filing of a petition for exemption should be published in the Federal Register and interested parties should be given an opportunity to comment. The Commission declines to adopt such an unprecedented procedure.

Management and Budget, Washington, DC 20503. Copies of the information collection submission to OMB are available from Joseph G. Salazar, Clearance Officer, Commodity Futures Trading Commission, 2033 K Street, NW., Washington, DC 20581. Telephone: (202) 254–9735.

B. Regulatory Flexibility Act

The Regulatory Flexibility Act ("RFA"), 5 U.S.C. 601 *et seq.*, requires that agencies, in proposing rules, consider the impact of those rules on small businesses. As the Commission noted in the preamble to the proposed rules, it has previously determined that neither futures commission merchants nor commodity pool operators should be considered small entities for purposes of the RFA. Specifically, the Commission found that with respect to futures commission merchants, based upon the fiduciary nature of futures commission merchant/customer relationships, as well as the requirement that futures commission merchants meet minimum financial requirements, futures commission merchants should be excluded from the definition of a small entity. With respect to commodity pool operators, Commission rule 4.13(a), 17 CFR 4.13(a) (1987), already exempts small entities from the regulatory requirements imposed on commodity pool operators.[43] Accordingly, the requirements of the RFA do not apply to those entities. For the same reasons, those entities required to register as futures commission merchants or commodity pool operators under this part should not be considered small entities.

With respect to introducing brokers and commodity trading advisors, and those required to register as such under these rules, the Commission stated that it is appropriate to evaluate within the context of a particular rule proposal whether some or all commodity trading advisors and introducing brokers should be considered to be small entities and, if so, to analyze the economic impact on such entities at that time. In this regard, the Commission noted that the regulations with respect to commodity trading advisors and introducing brokers are essentially the same as those governing these categories of registrant in connection with their activities relating to futures contracts and options traded or executed on or subject to the rules of a contract market designated by the Commission. Further, the Commission has previously found that its regulations governing these categories of registrant will not have a significant economic impact on a substantial number of small entities.[44] Therefore, pursuant to section 3(a) of the RFA, 5 U.S.C. 605(b), the Chairman certifies that these regulations will not have a significant economic impact on a substantial number of small entities.

[43] *See* 47 FR 18618 (April 30, 1982).

[44] 48 FR 35248 (August 3, 1983).

List of Subjects

17 CFR Part 1

Commodity futures, Financial requirements, Reporting and recordkeeping requirements, Customer protection, Definitions, Foreign futures, Foreign options, Registration requirements, Risk disclosure statements, Segregated funds, Introducing brokers.

17 CFR Part 30

Reporting and recordkeeping requirements, Customer protection, Definitions, Foreign futures, Foreign options, Registration requirements, Risk disclosure statements, Treatment of foreign futures and options secured amount.

17 CFR Part 32

Commodity options, Foreign options, Fraud.

17 CFR Part 166

Authorization to trade, Customer protection.

In consideration of the foregoing, and pursuant to the authority contained in the Commodity Exchange Act and, in particular, sections 2(a)(1), 4, 4a, 4b, 4c, 4d, 4e, 4f, 4g, 4h, 4i, 4j, 4k, 4l, 4m, 4n, 4o, 5, 5a, 6(a), 6(b), 6b, 6c, 8, 8a, 8c, 12, 15, 17, 19 and 20 thereof, 7 U.S.C. 2, 2a, 4, 6, 6a, 6b, 6c, 6d, 6e, 6f, 6g, 6h, 6i, 6j, 6k, 6l, 6m, 6n, 6o, 7, 7a, 8, 9, 12, 12a, 12c, 13a, 13a–1, 16, 19, 21, 23 and 24 (1982), and pursuant to the authority contained in 5 U.S.C. 552 and 552b (1982), the Commission hereby amends Chapter I of Title 17 of the Code of Federal Regulations as follows:

PART 1—GENERAL REGULATIONS UNDER THE COMMODITY EXCHANGE ACT

1. The authority citation for Part 1 continues to read as follows:

Authority: Sections 2(a)(1), 4, 4a, 4b, 4c, 4d, 4e, 4f, 4g, 4h, 4i, 4j, 4k, 4l, 4m, 4n, 4o, 5, 5a, 6(a), 6(b), 6b, 6c, 8, 8a, 8c, 12, 15, 17 and 20 of the Commodity Exchange Act, 7 U.S.C. 2, 2a, 4, 6, 6a, 6b, 6c, 6d, 6e, 6f, 6g, 6h, 6i, 6j, 6k, 6l, 6m, 6n, 6o, 7, 7a, 8, 9, 12, 12a, 12c, 13a, 13a–1, 16, 19, 21, and 24.

2. Section 1.3 is amended by adding paragraphs (rr) and (ss) to read as follows:

§ 1.3 Definitions.

* * * * *

(rr) *Foreign futures or foreign options secured amount.* This term means all money, securities and property held by or held for or on behalf of a futures commission merchant from, for, or on behalf of foreign futures or foreign options customers as defined in § 30.1 of this chapter:

(1) In the case of foreign futures customers, money, securities and property required by a futures commission merchant to margin, guarantee, or secure open foreign futures contracts plus or minus any unrealized gain or loss on such contracts; and

(2) In the case of foreign options customers in connection with open foreign options transactions money, securities and property representing premiums paid or received, plus any other funds required to guarantee or secure open transactions plus or minus any unrealized gain or loss on such transactions.

(ss) *Foreign board of trade.* This term means any board of trade, exchange or market located outside the United States, its territories or possessions, whether incorporated or unincorporated, where foreign futures or foreign options transactions are entered into.

3. Section 1.10 is amended by revising paragraphs (d)(1), (d)(2) and (g)(2) to read as follows:

§ 1.10 Financial Reports of Futures Commission Merchants and Introducing Brokers.

* * * * *

(d) *Contents of financial reports.* (1) Each form 1–FR filed pursuant to this § 1.10 which is not required to be certified by an independent public accountant must be completed in accordance with the instructions to the form and contain:

(i) A statement of financial condition as of the date for which the report is made;

(ii) A statement of changes in ownership equity for the period between the date of the most recent statement of financial condition filed with the Commission and the date for which the report is made;

(iii) A statement of the computation of the minimum capital requirements pursuant to § 1.17 as of the date for which the report is made;

(iv) For a futures commission merchant only, a schedule of segregation requirements and funds on deposit in segregation as of the date for which the report is made; and

(v) For a futures commission merchant only, a schedule of funds required to be on deposit and funds actually on deposit in separate accounts in accordance with § 30.7 of this chapter as of the date for which the report is made; and

(vi) In addition to the information expressly required, such further material information as may be necessary to make the required statements and schedules not misleading.

(2) Each form 1-FR filed pursuant to this § 1.10 which is required to be certified by an independent public accountant must be completed in accordance with the instructions to the form and contain:

(i) A statement of financial condition as of the date for which the report is made;

(ii) Statements of income (loss), changes in financial position, changes in ownership equity, and changes in liabilities subordinated to claims of general creditors, for the period between the date of the most recent certified statement of financial condition filed with the Commission and the date for which the report is made: *Provided*, That, for an applicant filing pursuant to paragraph (a)(2) of this section the period must be the year ending as of the date of the statement of financial condition;

(iii) A statement of the computation of the minimum capital requirements pursuant to § 1.17 as of the date for which the report is made;

(iv) For a futures commission merchant only, a schedule of segregation requirements and funds on deposit in segregation as of the date for which the report is made;

(v) For a futures commission merchant only, a schedule of funds required to be on deposit and funds actually on deposit in separate accounts in accordance with § 30.7 of this chapter as of the date for which the report is made;

(vi) Appropriate footnote disclosures; and

(vii) In addition to the information expressly required, such further material information as may be necessary to make the required statements not misleading.

* * * * *

(g) * * *

(2) All of the copies of the Financial and Operational Combined Uniform Single Report under the Securities Exchange Act of 1934, Part II or Part IIA, filed pursuant to paragraph (h) of this section will be public: *Provided, however*, That if the statement of financial condition, the computation of net capital, and the schedule (to be filed by a futures commission merchant only) of segregation requirements and funds on deposit in segregation and the schedule (to be filed by a futures commission merchant only) of funds required to be on deposit and funds actually on deposit in separate accounts in accordance with § 30.7 of this chapter are bound separately from the other financial statements (including the statement of income (loss)), footnote disclosures and schedules of the Financial and Operational Combined Uniform Single Report under the Securities and Exchange Act of 1934, Part II or Part IIA, trade secrets and certain other commercial or financial information on such other statements and schedules will be treated as nonpublic for purposes of the Freedom of Information Act and the Government in the Sunshine Act and Parts 145 and 147 of this chapter.

* * * * *

4. Section 1.12 is amended by revising paragraph (b)(2) to read as follows:

§ 1.12 Maintenance of Minimum Financial Requirements by Futures Commission Merchants and Introducing Brokers.

* * * * *

(b) * * *

(2) 6 percent of the following amount: The customer funds required to be segregated pursuant to the Act and these regulations and foreign futures or foreign options secured amount, less the market value of commodity options purchased by such customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however*, That the deduction for each such customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amounts; or

* * * * *

4. Section 1.16 is amended by revising paragraph (a)(4) to read as follows:

§ 1.16 Qualifications and Reports of Accountants

(a) * * *

(4) *Customer*. The term "customer" means customer (as defined in § 1.3(k)) and option customer (as defined in § 1.3(jj) and in § 32.1(c) of this chapter) and includes a foreign futures and foreign options customer (as defined in § 30.1(c) of this chapter).

* * * * *

5. Section 1.17 is amended by revising paragraphs (a)(1)(i)(B), (b)(2), (c)(5) (iii), (e)(1), (h)(2)(vi)(C), (h)(2)(vii)(A), (h)(2)(vii)(B), (h)(2)(viii)(A), (h)(3)(ii) and (h)(3)(v) to read as follows:

§ 1.17 Minimum financial requirements for futures commission merchants and introducing brokers.

(a) * * *

(1) * * *

(i) * * *

(B) Four percent of the following amount: the customer funds required to be segregated pursuant to the Act and these regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however*, That the deduction for each customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amounts; or

* * * * *

(b) * * *

(2) "Customer" means customer (as defined in § 1.3(k)), option customer (as defined in § 1.3(jj) and in § 32.1(c) of this chapter) and includes a foreign futures and foreign options customer (as defined in § 30.1(c) of this chapter).

* * * * *

(c) * * *

(5) * * *

(iii) In the case of a futures commission merchant, four percent of the market value of commodity options granted (sold) by option customers on or subject to the rules of a contract market or a foreign board of trade.

* * * * *

(e) * * *

(1) Either adjusted net capital of any of the consolidated entities would be less than the greatest of:

(i) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(ii)(A) of this section;

(ii) For a futures commission merchant or applicant therefor, 7 percent of the following amount: the customer funds required to be segregated pursuant to the Act and these regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however*, That the deduction for each customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amounts; or

(iii) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1(e) of the

Securities and Exchange Commission (17 CFR 240.15c3-1(e)); or

* * * * *

(h) * * *

(2) * * *

(vi) * * *

(C) The secured demand note agreement may also provide that, in lieu of the procedures specified in the provisions required by paragraph (h)(2)(vi)(B) of this section, the lender, with the prior written consent of the applicant and the National Futures Association, or with the prior written consent of the registrant and the designated self-regulatory organization or, if the registrant is not a member of a designated self-regulatory organization, the Commission, may reduce the unpaid principal amount of the secured demand note: *Provided*, That after giving effect to such reduction the adjusted net capital of the applicant or registrant would not be less than the greatest of:

(*1*) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(ii)(A) of this section;

(*2*) For a futures commission merchant or applicant therefor, 7 percent of the following amount: the customer funds required to be segregated pursuant to the Act and these regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however*, That the deduction for each customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amounts; or

(*3*) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(b)(6)(iii) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(b)(6)(iii)): *Provided, further*, That no single secured demand note shall be permitted to be reduced by more than 15 percent of its original principal amount and after such reduction no excess collateral may be withdrawn.

(vii) *Permissive prepayments and special prepayments.* (A) An applicant or registrant at its option, but not at the option of the lender, may, if the subordination agreement so provides, make a payment of all or any portion of the payment obligation thereunder prior to the scheduled maturity date of such payment obligation (hereinafter referred to as a "prepayment"), but in no event may any prepayment be made before the expiration of one year from the date such subordination agreement became effective: *Provided, however*, That the foregoing restriction shall not apply to temporary subordination agreements which comply with the provisions of paragraph (h)(3)(v) of this section nor shall it apply to "special prepayments" made in accordance with the provisions of paragraph (h)(2)(vii)(B) of this section. No prepayment shall be made if, after giving effect thereto (and to all payments of payment obligations under any other subordination agreements then outstanding, the maturity or accelerated maturities of which are scheduled to fall due within six months after the date such prepayment is to occur pursuant to this provision, or on or prior to the date on which the payment obligation in respect to such prepayment is scheduled to mature disregarding this provision, whichever date is earlier) without reference to any projected profit or loss of the applicant or registrant, the adjusted net capital of the applicant or registrant is less than the greatest of:

(*1*) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(ii)(A) of this section;

(*2*) For a futures commission merchant or applicant therefor, 7 percent of the following amount: the customer funds required to be segregated pursuant to the Act and these regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however*, That the deduction for each customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amounts; or

(*3*) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(b) (7) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(b) (7)). Notwithstanding the above, no prepayment shall occur without the prior written approval of the National Futures Association, in the case of an applicant, or without the prior written approval of the designated self-regulatory organization, if any, and the Commission, in the case of a registrant.

(B) An applicant or registrant at its option, but not at the option of the lender, may, if the subordination agreement so provides, make a payment at any time of all or any portion of the payment obligation thereunder prior to the scheduled maturity date of such payment obligation (hereinafter referred to as a "special prepayment"). No special prepayment shall be made if, after giving effect thereto (and to all payments of payment obligations under any other subordination agreements then outstanding, the maturity or accelerated maturities of which are scheduled to fall due within six months after the date such special prepayment is to occur pursuant to this provision, or on or prior to the date on which the payment obligation in respect to such special prepayment is scheduled to mature disregarding this provision, whichever date is earlier) without reference to any projected profit or loss of the applicant or registrant, the adjusted net capital of the applicant or registrant is less than the greatest of:

(*1*) 200 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(ii)(A) of this section;

(*2*) For a futures commission merchant or applicant therefor, 10 percent of the following amount: the customer funds required to be segregated pursuant to the Act and these regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however*, That the deduction for each customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amounts; or

(*3*) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3-1d(c)(5)(ii) of the Securities and Exchange Commission (17 CFR 240.15c3-1d(c)(5)(ii)): *Provided, further*, That no special prepayment shall be made if pre-tax losses during the latest three-month period were greater than 15 percent of current excess adjusted net capital. Notwithstanding the above, no special prepayment shall occur without the prior written approval of the National Futures Association, in the case of an applicant, or without the prior written approval of the designated self-regulatory organization, if any, and the Commission, in the case of a registrant.

(viii) *Suspended repayment.* (A) The payment obligation of the applicant or registrant in respect of any subordination agreement shall be suspended and shall not mature if, after giving effect to payment of such payment obligation (and to all payments of payment obligations of the applicant or registrant under any other subordination agreement(s) then outstanding which are scheduled to mature on or before such payment obligation), the adjusted net capital of the applicant or registrant would be less than the greatest of:

(*1*) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(ii)(A) of this section;

(*2*) For a futures commission merchant or applicant therefor, 6 percent of the following amount: the customer funds required to be segregated pursuant to the Act and these regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however,* That the deduction for each customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amounts; or

(*3*) for an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(b)(8)(i) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(b)(8)(i)): *Provided,* That the subordination agreement may provide that if the payment obligation of the applicant or registrant thereunder does not mature and is suspended as a result of the requirement of this paragraph (h)(2)(viii) for a period of not less than six months, the applicant or registrant shall then commence the rapid and orderly liquidation of its business, but the right of the lender to receive payment, together with accrued interest or compensation, shall remain subordinate as required by the provisions of this section.

* * * * *

(3) * * *

(ii) *Notice of maturity or accelerated maturity.* Every applicant or registrant shall immediately notify the National Futures Association, and the registrant shall immediately notify the designated self-regulatory organization, if any, and the Commission if, after giving effect to all payments of payment obligations under subordination agreements then outstanding which are then due or mature within the following six months without reference to any projected profit or loss of the applicant or registrant, its adjusted net capital would be less than:

(A) 120 percent of the minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(ii)(A) of this section;

(B) For a futures commission merchant or applicant therefor, 6 percent of the following amount: The customer funds required to be segregated pursuant to the Act and these regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however,* That the deduction for each customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amount; or

(C) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(c)(2) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(c)(2)).

* * * * *

(v) *Temporary subordinations.* To enable an applicant or registrant to participate as an underwriter of securities or undertake other extraordinary activities and remain in compliance with the adjusted net capital requirements of this section, an applicant or registrant shall be permitted, on no more than three occasions in any 12-month period, to enter into a subordination agreement on a temporary basis which has a stated term of no more than 45 days from the date the subordination agreement became effective: *Provided,* That this temporary relief shall not apply to any applicant or registrant if the adjusted net capital of the applicant or registrant is less than the greatest of:

(A) 120 percent of the appropriate minimum dollar amount required by paragraphs (a)(1)(i)(A) or (a)(1)(ii)(A) of this section;

(B) For a futures commission merchant or applicant therefor, 7 percent of the following amount: the customer funds required to be segregated pursuant to the Act and these regulations and the foreign futures or foreign options secured amount, less the market value of commodity options purchased by customers on or subject to the rules of a contract market or a foreign board of trade: *Provided, however,* That the deduction for each customer shall be limited to the amount of customer funds in such customer's account(s) and foreign futures and foreign options secured amounts;

(C) For an applicant or registrant which is also a securities broker or dealer, the amount of net capital specified in Rule 15c3–1d(c)(5)(i) of the Securities and Exchange Commission (17 CFR 240.15c3–1d(c)(5)(i)); or (D) the amount of equity capital as defined in paragraph (d) of this section is less than the limits specified in paragraph (d) of this section. Such temporary subordination agreement shall be subject to all the other provisions of this section.

* * * * *

6. Section 1.19 is revised to read as follows:

§ 1.19 Prohibited Trading in Certain "Puts" and "Calls".

No futures commission merchant or introducing broker may make, underwrite, issue, or otherwise assume any financial responsibility for the fulfillment of, any commodity option except:

(a) Commodity options traded on or subject to the rules of a contract market in accordance with the requirements of Part 33 of this chapter; or

(b) Commodity options traded on or subject to the rules of a foreign board of trade in accordance with the requirements of Part 30 of this chapter.

7. Section 1.33 is amended by revising paragraphs (a) and the introductory paragraph of paragraph (b) to read as follows:

§ 1.33 Monthly and Confirmation Statements.

(a) Monthly Statements. Each futures commission merchant must promptly furnish in writing to each commodity customer and to each option customer and to each foreign futures and foreign options customer, as of the close of the last business day of each month or as of any regular monthly date selected, except for accounts in which there are neither open positions at the end of the statement period nor any changes to the account balance since the prior statement period, but in any event not less frequently than once every three months, a statement which clearly shows:

(1) For each commodity customer and foreign futures customer—

(i) The open contracts with prices at which acquired;

(ii) The net unrealized profits or losses in all open contracts marked to the market; and

(iii) Any customer funds carried with the futures commission merchant; and

(iv) A detailed accounting of all financial charges and credits to such customer accounts during the monthly reporting period, including all customer funds and funds on deposit with respect to foreign futures transactions in accordance with § 30.7 of this chapter received from or disbursed to such customer and realized profits and losses; and

(2) For each option customer and foreign options customer—

(i) All commodity options and foreign options purchased, sold, exercised, or expired during the monthly reporting period, identified by underlying futures contract or underlying physical, strike price, transaction date, and expiration date;

(ii) The open commodity option and foreign option positions carried for such customer as of the end of the monthly reporting period, identified by underlying futures contract or underlying physical, strike price, transaction date, and expiration date;

(iii) All open commodity option and foreign option positions marked to the market and the amount each position is in the money, if any;

(iv) Any customer funds carried in such customer's account(s); and

(v) A detailed accounting of all financial charges and credits to such customer's account(s) during the monthly reporting period, including all customer funds and funds on deposit with respect to foreign options transactions received from or disbursed to such customer, premiums charged and received, and realized profits and losses.

(b) Confirmation statement. Each futures commission merchant must, not later than the next business day after any commodity futures or commodity option transaction, including any foreign futures or foreign options transactions, furnish:

* * * * *

8. 17 CFR Part 30 is amended by revising the Part heading, by revising and redesignating § 30.02 as § 30.9 and by adding §§ 30.1–30.8 and 30.10–30.11 to read as follows:

PART 30—FOREIGN FUTURES AND FOREIGN OPTIONS TRANSACTIONS

Authority: Secs. 2(a)(1)(A), 4, 4c and 8a of the Commodity Exchange Act, 7 U.S.C. 2, 4, 6, 6c and 12a (1982).

§ 30.1 Definitions.

For the purposes of this part:

(a) "Foreign futures" means any contract for the purchase or sale of any commodity for future delivery made, or to be made, on or subject to the rules of any foreign board of trade.

(b) "Foreign option" means any transaction or agreement which is or is held out to be of the character of, or is commonly known to the trade as, an "option", "privilege", "indemnity", "bid", "offer", "put", "call", "advance guaranty" or "decline guaranty", made or to be made on or subject to the rules of any foreign board of trade.

(c) "Foreign futures or foreign options customer" means any person located in the United States, its territories or possessions who trades in foreign futures or foreign options: *Provided*, That an owner or holder of a proprietary account as defined in paragraph (y) of § 1.3 of this chapter shall not be deemed to be a foreign futures or foreign options customer within the meaning of §§ 30.6 and 30.7 of this part.

§ 30.2 Applicability of the Act and rules.

(a) Except as specified in this part or unless the context otherwise requires, the provisions of sections 2(a)(1), 4, 4c, 4f, 4g, 4k, 4l, 4m, 4n, 4o, 4p, 6, 6c, 6d, 8, 8a, 9, 12, 13, and 14 of the Act and parts 1, 3, 4, 10, 11, 12, 13, 14, 21, 155, 166 and 190 of this chapter shall apply to the persons and transactions that are subject to the requirements of this part as though they were set forth herein and included specific references to foreign board of trade, foreign futures, foreign options, foreign futures and foreign options customers, and foreign futures and foreign options secured amount, as appropriate.

(b) The provisions of §§ 1.20 through 1.30, 1.32, 1.35(a) (2)–(4) and (c)–(i), 1.36(b), 1.38, 1.39, 1.40 through 1.51, 1.53, 1.54, 1.55, 1.58, 1.59, 33.2 through 33.6 and Parts 15 through 20 of this chapter shall not be applicable to the persons and transactions that are subject to the requirements of this part.

§ 30.3 Prohibited transactions.

(a) It shall be unlawful for any person to engage in the offer and sale of any foreign futures contract or foreign options transaction for or on behalf of a foreign futures or foreign options customer, except in accordance with the provisions of this part: *Provided*, That, notwithstanding any other provisions of this part, it shall be unlawful for any person to engage in the offer and sale of any foreign option until the Commission, by order, authorizes such foreign option to be offered in the United States: *And, provided further*, That, with the exception of the disclosure and antifraud provisions set forth in §§ 30.6 and 30.9 of this part, the provisions of this part shall not apply to transactions executed on a foreign board of trade, and carried for or on behalf of a customer at a designated contract market, subject to an agreement with and rules of a contract market which permit positions in a commodity interest which have been established on one market to be liquidated on another market.

(b) Except as otherwise provided in § 30.4 of this part or pursuant to an exemption granted under § 30.10 of this part, it shall be unlawful for any person to engage in the offer and sale of any foreign futures contract or foreign option transaction for or on behalf of any foreign futures or foreign options customer other than by or through a futures commission merchant on a fully-disclosed basis.

§ 30.4 Registration required.

Except as provided in § 30.5 of this part, it shall be unlawful for any person, with respect to a foreign futures or foreign options customer:

(a) To solicit or accept orders for or involving any foreign futures contract or foreign options transaction and, in connection therewith, to accept any money, securities or property (or extend credit in lieu thereof) to margin, guarantee or secure any trades or contracts that result or may result therefrom unless such person shall have registered, under the Act, with the Commission as a futures commission merchant and such registration shall not have expired nor been suspended nor revoked;

(b) Except an individual who elects to be and is registered as an associated person of a futures commission merchant, to solicit or accept orders for or involving any foreign futures contract or foreign options transaction, and who in connection therewith, does not accept any money, securities, or property (or extend credit in lieu thereof) to margin, guarantee, or secure any trade or contracts that result or may result therefrom, unless such person shall have registered, under the Act, with the Commission as an introducing broker and such registration shall not have expired nor been suspended nor revoked;

(c) To engage in a business which is of the nature of an investment trust, syndicate, or similar form of enterprise, and, in connection therewith, to solicit, accept, or receive funds, securities, or property, either directly or through capital contributions, the sale of stock or other forms of securities, or otherwise, for the purpose of trading, directly or indirectly, in any foreign futures contract or foreign options transaction unless such person shall have registered, under the Act, with the Commission as a commodity pool operator and such registration shall not have expired nor been suspended nor revoked: *Provided, however,* That the registration requirement set forth in this paragraph shall not apply to any investment trust, syndicate, or similar form of enterprise located outside the United States, its territories or possessions which is registered as an investment company under the Investment Company Act of 1940 and whose securities are registered in accordance with the Securities Act of 1933, or which is otherwise exempt from such registration requirements: *And, provided further,* That no more than 10% of the participants in, and the value of the assets of, such investment trust, syndicate or similar form of enterprise located outside the United States, its territories or possessions, are held by or on behalf of foreign futures and foreign options customers.

(d) To solicit or enter into an agreement to direct, or to guide such customer's account by means of a systematic program that recommends specific transactions in any foreign option or foreign futures contract unless such person shall have registered, under the Act, with the Commission as a commodity trading advisor and such registration shall not have expired nor been suspended nor revoked: *Provided,* That the term "commodity trading advisor" does not include (i) any bank or trust company or any person acting as an employee thereof, (ii) any news reporter, news columnist, or news editor of the print or electronic media, or any lawyer, accountant, or teacher, (iii) the publisher or producer of any print or electronic data of general and regular dissemination, including its employees, (iv) the named fiduciary, or trustee, of any defined benefit plan which is subject to the provisions of the Employee Retirement Income Security Act of 1974, or any fiduciary whose sole business is to advise that plan, (v) any foreign board of trade or clearing organization of such board of trade, (vi) an insurance company subject to regulation by any State, or any wholly-owned subsidiary or employee thereof, and (vii) such other persons not within the intent of the term "commodity trading advisor" as the Commission may specify by rule, regulation, or order: *And, provided further,* That the furnishing of such services by the foregoing persons is solely incidental to the conduct of their business or profession. Registration as a commodity trading advisor shall not be required if such person is registered with the Commission as a futures commission merchant, introducing broker, commodity pool operator or associated person, or is otherwise exempt from registration pursuant to § 30.5.

(e) Any person required to be registered as a futures commission merchant under this section must maintain an office in the United States which is managed by an individual domiciled in the United States and registered with the Commission as an associated person.

§ 30.5 Alternative procedures for non-domestic persons.

(a) *Agent for service of process.* Any person not located in the United States, its territories or possessions, who is required in accordance with the provisions of this part to be registered with the Commission, other than a person required to be registered as a futures commission merchant, will be exempt from such registration requirement if such person enters into a written agency agreement with the futures commission merchant through which business is done in accordance with the provisions of § 30.3(b) of this part, with any registered futures association or any other person located in the United States in the business of providing such services, pursuant to which agreement such futures commission merchant or other person is authorized to serve as the agent of such person for purposes of accepting delivery and service of communications issued by or on behalf of the Commission, U.S. Department of Justice, any self-regulatory organization or any foreign futures or foreign options customer. If the written agency is entered into with any person other than the futures commission merchant through which business is done, such futures commission merchant must be expressly identified in such agency agreement. Service or delivery of any communication issued by or on behalf of the Commission, U.S. Department of Justice, any self-regulatory organization or any foreign futures or foreign options customer, pursuant to such agreement shall constitute valid and effective service or delivery upon such person. Unless otherwise specified by the Commission, the agreement required by this section shall be filed with the Vice President-Registration, National Futures Association, 200 West Madison Street, Chicago, Illinois 60606, with a copy to the Vice President-Compliance, National Futures Association. For the purposes of this section, the term "communication" includes any summons, complaint, order, subpoena, request for information, or notice, as well as any other written document or correspondence relating to any activities of such person subject to regulation under this part.

(b) *Termination of agreement.* Whenever the agreement referred to in paragraph (a) of this section is terminated or is otherwise no longer in effect, the futures commission merchant or any other person which is party to the agreement shall immediately notify the Vice President-Compliance of the National Futures Association and the futures commission merchant through which business is done, as appropriate. Upon notice, a futures commission merchant shall not accept from the person that has entered into such agreement any order, other than liquidating order(s), for, or on behalf of a foreign futures or foreign options customer. Notwithstanding the termination of the agreement referred to in paragraph (a) of this section, service or delivery of any communication issued by or on behalf of the Commission, U.S. Department of Justice, any self-regulatory organization or any foreign futures or foreign options customer pursuant to the agreement shall nonetheless constitute valid and effective service or delivery upon such person with respect to any transaction entered into on or before the date of the termination of the agreement.

(c) *Applicability of other rules.* Any person who is located outside of the United States, its territories or possessions, and who, in accordance with the provisions of paragraph (a) of this section, is exempt from registration as an introducing broker, commodity pool operator or commodity trading advisor under this part, shall nonetheless comply with the provisions of §§ 30.6 of this part and 1.37 and 1.57 of this chapter as if registered in such capacity.

(d) *Access to records.* Any person exempt from registration with the Commission in accordance with the provisions of paragraph (a) of this section must, upon the request of any representative of the Commission or U.S. Department of Justice, provide such records as such person is required to maintain under this part as requested at the place in the United States designated by the representative within 72 hours after the person receives the request.

§ 30.6 Disclosure.

(a) *Futures commission merchants and introducing brokers.* (1) No futures commission merchant or, in the case of an introduced account, no introducing broker may open a foreign futures or foreign options account for a foreign futures or foreign options customer unless the futures commission merchant or introducing broker first delivers to the customer either in the customer account agreement or on a separate form the following risk disclosure statement set in bold-face type or print:

Risk Disclosure Statement

Foreign Futures and Foreign Options

The risk of loss in trading foreign futures and foreign options can be substantial. Therefore, you should carefully consider whether such trading is suitable for you in light of your financial condition. In considering whether to trade foreign futures or foreign options, you should be aware of the following:

(1) Participation in foreign futures and foreign options transactions involves the execution and clearing of trades on or subject to the rules of a foreign board of trade.

(2) Neither the Commodity Futures Trading Commission, the National Futures Association nor any domestic exchange regulates activities of any foreign boards of trade, including the execution, delivery and clearing of transactions, or has the power to compel enforcement of the rules of a foreign board of trade or any applicable foreign laws. Generally, the foreign transaction will be governed by applicable foreign law. This is true even if the exchange is formally linked to a domestic market so that a position taken on the market may be liquidated by a transaction on another market. Moreover, such laws or regulations will vary depending on the foreign country in which the foreign futures or foreign options transaction occurs.

(3) For these reasons, customers who trade foreign futures or foreign options contracts may not be afforded certain of the protective measures provided by the Commodity Exchange Act, the Commission's regulations and the rules of the National Futures Association and any domestic exchange, including the right to use reparations proceedings before the Commission and arbitration proceedings provided by the National Futures Association or any domestic futures exchange. In particular, funds received from customers for foreign futures or foreign options transactions may not be provided the same protections as funds received in respect of transactions on United States futures exchanges. Therefore, you should obtain as much information as possible from your account executive concerning the foreign rules which will apply to your particular transaction.

(4) You should also be aware that the price of any foreign futures or foreign options contract and, therefore, the potential profit and loss thereon, may be affected by any variance in the foreign exchange rate between the time your order is placed and the time it is liquidated, offset or exercised.

(2) If a futures commission merchant or introducing broker, or any associated person of such futures commission merchant or introducing broker, has received general discretionary authority to engage in foreign futures or foreign options transactions on behalf of a foreign futures or foreign options customer, the futures commission merchant or introducing broker must receive a separate acknowledgment signed and dated by the customer that the customer has received and understood the foreign futures and options risk disclosure statement.

(b) *Commodity pool operators and commodity trading advisors.* (1) No commodity pool operator registered or required to be registered under this part, or exempt from registration pursuant to § 30.5 of this part, may, directly or indirectly, solicit, accept or receive funds, securities or other property from a prospective participant in a foreign pool that it operates or that it intends to operate or, in the case of a commodity trading advisor, no commodity trading advisor registered or required to be registered under this part, or exempt from registration pursuant to § 30.5 of this part, may solicit or enter into an agreement with a prospective client to direct or to guide the client's foreign commodity interest trading by means of a systematic program that recommends specific transactions, unless the commodity pool operator or commodity trading advisor, at or before the time it engages in such activities, first complies with the provisions of paragraph (a)(1) of this section.

(2) The disclosure statement required to be made in paragraph (b)(1) above may be given as a separate document or, if a part of the Disclosure Document required to be furnished customers or potential customers pursuant to §§ 4.21(a) or 4.31(a) of this chapter, must be the only language on the page(s) immediately following the disclosure required to be made by §§ 4.21(a)(17) and 4.31(a)(8) of this chapter.

(c) The acknowledgment required by paragraphs (a) and (b) of this section must be retained by the futures commission merchant, introducing broker, commodity pool operator or commodity trading advisor in accordance with § 1.31 of this chapter.

(d) This section does not relieve a futures commission merchant or introducing broker from its obligations under § 33.7 of this chapter: *Provided, however,* That a new disclosure statement is not required to be furnished if the futures commission merchant or introducing broker has previously delivered such statement to the foreign options customer in connection with the opening of a commodity option account under part 33 of this chapter.

(e) This section does not relieve a futures commission merchant, introducing broker, commodity pool operator or commodity trading advisor from any other disclosure obligation it may have under applicable law or regulation.

§ 30.7 Treatment of foreign futures or foreign options secured amount.

(a) Except as provided in this section, a futures commission merchant must maintain in a separate account or accounts money, securities and property in an amount at least sufficient to cover or satisfy all of its current obligations to foreign futures or foreign options customers denominated as the foreign futures or foreign options secured amount. Such money, securities and property may not be commingled with the money, securities or property of such futures commission merchant, with any proprietary account of such futures commission merchant, or used to secure or guarantee the obligations of, or extend credit to, such futures commission merchant or any proprietary account of such futures commission merchant.

(b) A futures commission merchant may deposit together with the secured amount required to be on deposit in the separate account or accounts referred to in paragraph (a) of this section money, securities or property held for or on behalf of other customers of the futures commission merchant for the purpose of entering into foreign futures or foreign options transactions. In such a case, the amount that must be deposited in such separate account or accounts must be no less than the greater of (i) the foreign futures and foreign options secured amount plus the amount that would be required to be on deposit if all such customers were foreign futures or foreign options customers under this part 30, or (ii) the foreign futures or foreign options secured amount plus the amount required to be held in a separate account or accounts for or on behalf of customers pursuant to any law, or rule, regulation or order thereunder, or any rule of any self-regulatory organization authorized thereunder, in the jurisdiction in which the depository or the customer, as appropriate, is located.

(c) The separate account or accounts referred to in paragraph (a) of this section must be maintained under an account name that clearly identifies them as such, with any of the following depositories:

(i) A bank or trust company located in the United States or as designated;

(ii) Another person registered as a futures commission merchant;

(iii) The clearing organization of any foreign board of trade;

(iv) Any member of such board of trade; or

(v) Such member or clearing organization's designated depositories. Each futures commission merchant must obtain and retain in its files for the period provided in § 1.31 of this chapter an acknowledgment from such depository that it was informed that such money, securities or property are held for or on behalf of foreign futures and foreign options customers and are being held in accordance with the provisions of these regulations.

(d) In no event may money, securities or property representing the foreign futures or foreign options secured amount be held or commingled and deposited with customer funds in the same account or accounts required to be separately accounted for and segregated pursuant to section 4d of the Act and the regulations thereunder.

(e) Each futures commission merchant which invests money, securities or property on behalf of foreign futures or foreign options customers shall keep a record showing the following:

(i) The date on which such investments were made;

(ii) The name of the person through whom such investments were made;

(iii) The amount of money so invested;

(iv) A description of the obligations in which such investments were made;

(v) The identity of the depositories or other places where such obligations are maintained;

(vi) The date on which such investments were liquidated or otherwise disposed of and the amount of money received of such disposition, if any; and

(vii) The name of the person to or through whom such investments were disposed of.

(f) Each futures commission merchant must compute as of the close of each business day:

(1) The total amount of money, securities and property on deposit in separate account(s) in accordance with this section;

(2) The total amount of money, securities and property required to be on deposit in separate account(s) in accordance with this section; and

(3) The amount of the futures commission merchant's residual interest in money, securities and property on deposit in separate account(s) in accordance with this section. Such computations must be completed prior to noon on the next business day and must be kept, together with all supporting data, in accordance with the requirements of § 1.31.

§ 30.8 Quarterly reporting requirements.

(a) Each futures commission merchant required to be registered under this part shall file written quarterly reports on a form specified by the National Futures Association at the National Futures Association's headquarters office in Chicago, Illinois, by the tenth business day of the month following the quarter covered by the reports.

(b) Each report shall contain the following information separately for each foreign board of trade on which foreign futures contracts or foreign options transactions were effected:

(1) The total number of foreign futures contracts, separately by contract, long and short, customer or proprietary, executed during the quarter on such board of trade on behalf of the futures commission merchant or its foreign futures customers;

(2) The total number of foreign futures contracts, separately by contract, long and short, customer or proprietary, open on such board of trade on behalf of the futures commission merchant or its foreign futures customers as of the close of business on the last business day of the quarter;

(3) The total number of foreign options, separately by underlying futures contracts for options on futures contracts or by underlying physical for options on physicals, by put, by call, and by customer or proprietary, executed during the quarter on such board of trade on behalf of the futures commission merchant or its foreign options customers;

(4) The total number of foreign options, separately by underlying futures contracts for options on futures contracts or by underlying physical for options on physicals, by put, by call, and by customer or proprietary, open on such board of trade on behalf of the futures commission merchant or its foreign options customers as of the close of business on the last business day of the quarter.

§ 30.9 Fraudulent transactions prohibited.

It shall be unlawful for any person, by use of the mails or by any means or instrumentality of interstate commerce, directly or indirectly, in or in connection with any account, agreement or transaction involving any foreign futures contract or foreign options transaction:

(a) To cheat or defraud or attempt to cheat or defraud any other person;

(b) To make or cause to be made to any other person any false report or statement thereof or to enter or cause to be entered for any person any false record thereof;

(c) To deceive or attempt to deceive any other person by any means whatsoever in regard to any such account, agreement or transaction or the disposition or execution of any such account, agreement or transaction or in regard to any act of agency performed with respect to such account, agreement or transaction; or

(d) To bucket any order, or to fill any order by offset against the order or orders of any other person or without the prior consent of any person to become the buyer in respect to any selling order of such person, or become the seller in respect to any buying order of such person.

§ 30.10 Petitions for exemption.

Any person adversely affected by any requirement of this part may file a petition with the Secretary of the Commission, which petition must set forth with particularity the reasons why that person believes that he should be exempt from such requirement. The Commission may, in its discretion, grant such an exemption if that person demonstrates to the Commission's satisfaction that the exemption is not otherwise contrary to the public interest or to the purposes of the provision from which exemption is sought. The petition will be granted or denied on the basis of the papers filed. The petition may be granted subject to such terms and conditions as the Commission may find appropriate.

§ 30.11 Applicability of state law.

Pursuant to section 12(e)(2) of the Act, the provisions of any state law, including any rule or regulation thereunder, may be applicable to any person required to be registered under this part who solicits foreign futures and foreign options customers and who shall fail or refuse to obtain such registration, unless such person is exempt from such registration in accordance with the provisions of §§ 30.4, 30.5 or 30.10 of this part.

Appendix A–Part 30—Interpretative Statement With Respect to the Commission's Exemptive Authority Under Section 30.10 of Its Rules

Part 30 of the Commission's regulations establishes the regulatory structure governing the offer and sale in the United States of futures and options contracts made or to be made on or subject to the rules of a foreign board of trade. Section 30.10 of these regulations provides that, upon petition, the Commission may exempt any person from any requirement of this part. Specifically, section 30.10 states:

Any person adversely affected by any requirement of this part may file a petition with the Secretary of the Commission, which petition must set forth with particularity the reasons why that person believes that he should be exempt from such requirement. The Commission may, in its discretion, grant such an exemption if that person demonstrates to the Commission's satisfaction that the exemption is not otherwise contrary to the public interest or to the purposes of the provision from which exemption is sought. The petition will be granted or denied on the basis of the papers filed. The petition may be granted subject to such terms and conditions as the Commission may find appropriate.

As the provisions of this section make clear, any person subject to regulation under part 30 may petition the Commission for an exemption. In adopting these regulations, however, the Commission noted in particular that persons located outside the United States that solicit or accept orders directly from United States customers for foreign futures or options transactions and that are subject to a comparable regulatory scheme in the country in which they are located may apply under section 30.10 for exemption from some or all of the requirements that would otherwise be applicable to such persons. This interpretative statement sets forth the elements that the Commission intends to evaluate in determining whether a particular regulatory program may be found to be comparable to the Commission's program.

The Commission wishes to emphasize, however, that this interpretative statement is not all inclusive, and that information with respect to other aspects of a particular regulatory program may be submitted by a petitioner or requested by the Commission. In this connection, the Commission would have broad discretion to determine that the policies of any program element generally are met, notwithstanding the fact that the offshore program does not contain an element identical to that of the Commission's regulatory program and conversely may assess how particular elements are in fact applied by offshore authorities. Thus, for example, in order to find that a particular program is comparable, the regulations thereunder would have to be applicable to all United States customers, notwithstanding any exemptions that might otherwise be available to particular classes of customer located offshore. A petitioner, therefore, must set forth with particularity the factual basis for a finding of comparability and the reasons why such policies and purposes are met, notwithstanding differences of degree and kind in its regulatory program.

No exemptions of a general nature will be granted unless the persons to which the exemption is to be applied consent to submit to jurisdiction in the United States by designating an agent for service of process pursuant to the provisions of rule 30.5 with respect to any activities of such persons otherwise subject to regulation under this part and to notify the National Futures Association of the commencement or termination of business in the United States. In this connection, to be exempted, such person must further agree to respond to a request to confirm that it continues to do business in the United States.

Persons located outside the United States may seek an exemption on their own behalf or an exemption may be sought on a general basis through the governmental agency responsible for the implementation and enforcement of the regulatory program in question, or the self-regulatory organizations of which such persons are members. The appropriate petitioner is a matter of judgment and may be determined by the parties seeking the exemption. The Commission, however, notes that it will be able to address petitions more efficiently if they are filed by the governmental agency or self-regulatory organization responsible for the regulatory program.

In this connection, as will be discussed in more detail below, any exemption of a general nature based on comparability will be conditioned upon appropriate information sharing arrangements between the Commission and the relevant governmental agency and/or self-regulatory organization. Representations from the appropriate governmental agency with respect to the applicability of any blocking statutes that may prevent the sharing of information requested under private arrangements would also be considered. Finally, in considering an exemption request, the Commission will take into account the extent to which United States persons or contracts regulated by the Commission are permitted to engage in futures-related activities or be offered in the country from which an exemption is sought.

In the Commission's review, the minimum elements of a comparable regulatory program would include: (1) Registration, authorization or other form of licensing, fitness review or qualification of persons through which customer orders are solicited and accepted; (2) minimum financial requirements for those persons that accept customer funds; (3) protection of customer funds from misapplication; (4) recordkeeping and reporting requirements; (5) minimum sales practice standards, including disclosure of the risks of futures and opotions transactions and, in particular, the risk of transactions undertaken outside the jurisdiction of domestic law; and (6) compliance.

Qualification. Under domestic law, registration identifies to the Commission, the public and other governmental agencies the individuals and entities that are properly authorized to solicit and accept customer orders and are in good standing. Equally important, the procedure provides the Commission, through the National Futures Association, the opportunity to determine whether applicants are unfit to deal with the public. In this connection, the standards for determining whether a person through its principals is fit for registration with the Commission are set forth in section 8a(2)–8a(4) of the Act. Timely access to information as to a firm's good standing and the application by relevant authorities of membership and licensing criteria, as well as the criteria themselves, will be considered by the Commission in assessing comparability.

Minimum Financial Requirements. Minimum financial requirements for persons that handle customer funds serve at least three critical functions. First, they provide a cushion together with margin such that in the event of a default of a customer, the losses of that customer need not adversely affect the funds held on behalf of other customers. Second, they help ensure that the person has sufficient funds to operate its business and, therefore, is less likely to be tempted to misapply customer funds for its own purposes. Third, they ensure that the person holding customer funds has some financial stake in its business and, therefore, is serious in its intent. In assessing comparability, capital rules or their equivalent will be considered together with any provisions made for insuring customer losses, the scope of clearing guarantees and segregation or customer trust calculation and accounting requirements which, to the extent they cover undermargined accounts, can provide significant protection of one customer from another customer's losses.

Customer Funds. The Act requires the strict segregation of customer funds from those of the person holding such funds. One of the primary purposes of this requirement is to prevent the misapplication of those funds for purposes other than those intended by the customer, which may affect not only the customer but the market as a whole. The purpose of segregation is also to identify customer deposits as assets of the customer, rather than the firm, in order that in bankruptcy such funds are payable only to satisfy the carrying firm's obligations to such customers and not other obligations of the firm. In assessing comparability of protection of customer funds, the Commission will consider protections accorded customer funds in a bankruptcy under applicable law, as well as protection from fraud.

Recordkeeping and Reporting. Recordkeeping requirements have long been recognized as the linchpin of the Commission's regulatory scheme. Reporting and recordkeeping requirements assist in determining that a registrant is acting in accordance with the provisions of the Act and the rules, regulations and orders of the Commission thereunder. Similarly, reporting requirements ensure that customers are timely advised of the transactions that have been executed on their behalf, thus ensuring that they are aware of their positions in the markets and may object to any transactions that they believe are in error. The Commission will consider the types of records maintained, the ability through those records to trace funds and transactions, and the period of retention and accessibility of records under the information sharing arrangements discussed below in considering comparability.

Sales Practice Standards. In 1982, Congress reaffirmed the importance of minimum sales practice standards to protect customers from fraud or misrepresentation by requiring any futures association registered by the Commission to adopt and enforce rules governing the sales practices of its members. The Commission has consistently provided that written disclosure of the risks of futures and options trading is essential to ensure that potential customers are aware of these risks and are not otherwise misled and that other appropriate disclosure is made. The Commission will review the type and manner of disclosure given and the mechanisms for assuring the disclosure requirements are met and, in particular, the treatment of discretionary accounts for which, for example, Commission rule 166.2 requires particularized documentation of intent to confer discretion in the case of foreign futures and options transactions.

Compliance. Finally, in assessing comparability of a program, the Commission will examine the procedures employed by the governmental authority or the appropriate self-regulatory organization to audit for compliance with, and to take action as appropriate against those persons that violate, the requirements of that program.

Information Sharing. As noted above, any exemption of a general nature would also require an information sharing arrangement between the Commission and the appropriate governmental or self-regulatory organization to ensure Commission access to information on an as needed basis as may be necessary to fulfill its regulatory responsibilities. The information subject to these arrangements generally would be of a type necessary in the first instance to monitor domestic markets and to protect domestic customers trading on foreign markets.

Firm-specific information that is potentially relevant to protection of domestic customers engaged in foreign transactions could include the following: (1) Registration qualification status; (2) names of principals; (3) current capital; (4) location of customer funds; (5) address of main office and branches; (6) exchange and self-regulatory organization memberships; (7) the existence of any derogatory information such as that required to be disclosed on the Commission's Form 7–R; (8) notice of limitations imposed on activities; (9) notice of undersegregation or undercapitalization; (10) notice of misuse of customer funds; and (11) notice of sanctions or of expulsion from exchange or self-regulatory organization membership. The Commission believes that much of the above information would be public in the ordinary course in most jurisdictions. From time to time, the Commission also may need immediate access to financial information concerning risks posed to domestic firms by the carrying of foreign positions.

In addition to information that relates to the financial stability and creditworthiness of the firm, the Commission should have access to transaction-specific information that confirms the execution of orders and prices and facilitates tracing of customer funds. Such data could include records reflecting: (1) That an order has been received by a firm on behalf of one or more United States customers; (2) that an order has been executed on an exchange on behalf of one or more United States customers; (3) that funds to margin, guarantee or secure United States customer transactions have been received by a firm and deposited in an appropriate depository; and (4) the price at which a transaction was executed and general access to pricing information.

Again, such information is likely to be maintained in the ordinary course of business. Tracing of customer funds would be most essential in cases of insolvency where repatriation of funds is at issue.

The Commission may also seek relevant position data information, including the identity of the position holder and related positions, in connection with surveillance of a potential "market disruption." This is particularly true in the case of integrated markets.

The Commission wishes to emphasize that the information sharing arrangements discussed herein are not necessarily a substitute for, nor would they preclude, a more formal agreement or arrangement with respect to the sharing of information.

PART 32—REGULATION OF COMMODITY OPTION TRANSACTIONS

9. The authority citation for Part 32 continues to read as follows:

Authority: Sections 2(a)(1)(A), 4c and 8a of the Commodity Exchange Act, 7 U.S.C. 2, 6c and 12a (1982).

10. Section 32.1 is amended by revising paragraph (a) to read as follows:

§ 32.1 Definitions.

(a) *Scope.* The provisions of this Part, except for the provisions of §§ 32.8 and 32.9 which shall in any event apply to all commodity option transactions, shall apply to all commodity option transactions except for commodity option transactions conducted or executed on or subject to the rules of a contract market, or a foreign board of trade, pursuant to section 4c of the Act and the regulations promulgated thereunder.

* * * * *

11. Section 32.11 is amended by revising paragraph (b) to read as folows:

§ 32.11 Suspension of Commodity Option Transactions.

* * * * *

(b) The provisions of paragraph (a) of this section shall not apply to any commodity option transaction conducted in accordance with the provisions of § 32.4(a) of this part, or any commodity option transaction conducted on or subject to the rules of a contract market or a foreign board of trade in accordance with the provisions of section 4c of the Act and any rule, regulation or order promulgated thereunder.

* * * * *

PART 166—CUSTOMER PROTECTION RULES

12. The authority citation for Part 166 is revised to read as follows:

Authority: Sections 2(a)(1)(A), 4b, 4c, 4g, 4h, 4*l*, 4*o*, 8a, and 19 of the Commodity Exchange Act, 7 U.S.C. 4, 6b, 6c, 6g, 6h, 6*l*, 6*o*, 12a, and 23.

13. Section 166.1 is amended by revising paragraphs (b)(1) and (b)(2) to read as follows:

§ 166.1 Definitions.

* * * * *

(b) The term "commodity interest" as used in this part means—

(1) Any contract for the purchase or sale of any commodity for future delivery, traded on or subject to the rules of a contract market or a foreign board of trade.

(2) Any agreement or transaction subject to Commission regulation under section 4c of the Act, including any such contract or transaction made or to be made on or subject to the rules of a foreign board of trade; or

* * * * *

14. Section 166.2 is amended by revising paragraph (b) to read as follows:

§ 166.2 Authorization to trade.

* * * * *

(b) Authorized in writing the futures commission merchant, introducing broker or any of their associated persons to effect transactions in commodity interests for the account without the customer's specific authorization; *Provided, however,* That if such futures commission merchant, introducing broker or any of their associated persons is also authorized to effect transactions in foreign futures or foreign options without the customer's specific authorization, such authorization must be expressly documented.

Issued in Washington, DC, on July 23, 1987, by the Commission.

Jean A. Webb,

Secretary to the Commission.

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DEPARTMENT OF ENERGY

Federal Energy Regulatory Commission

18 CFR Parts 270, 271, 273, and 274

[Docket No. RM 87-31-000, et al.; Order No. 479]

Procedures for Determining High-Cost Natural Gas Produced From Tight Formations

Issued July 29, 1987.

AGENCY: Federal Energy Regulatory Commission, DOE.

ACTION: Final rule.

SUMMARY: The Federal Energy Regulatory Commission (Commission) is issuing a final rule describing procedures for determining high-cost natural gas produced from tight formations eligible for incentive prices pursuant to section 107(c)(5) of the Natural Gas Policy Act of 1978. Specifically, the Commission is revising its regulations to provide that a